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Politics this week

Oct 6th 2005
From The Economist print edition

Turkey and the EU

After a nerve-jangling day of diplomatic brinkmanship, talks formally began on admitting **Turkey** as the first member of the European Union whose population is mainly Muslim. Austria withdrew its objections after it became clear that Croatia, its ally, would also be allowed to start EU entry talks despite previous concerns over its record on war criminals. Turkey was also assured that it would not be forced into accepting Cyprus's admission into NATO. See article

Germany came closer to knowing who will lead the country as the Social Democrats and the Christian Democrats held talks on forming a coalition government. The CDU's Angela Merkel received a boost to her chances of becoming the country's next leader when her party picked up a seat in the eastern city of Dresden, where voting in last month's general election had been postponed because of the death of a candidate.

AFP

A report on the future status of **Kosovo**, launching a process that could lead to independence, was submitted to Kofi Annan, the UN secretary-general. Agreement over the province between Serbs and Albanians remained elusive, with some Albanians demanding immediate independence with no conditions. See article

Around 700 African migrants rushed barriers in an attempt to cross Morocco's border with the **Spanish enclave** of Melilla. Last week, five migrants died in a stampede at the border of Spain's other Moroccan enclave, Ceuta. Spain's interior minister pledged to build more, and higher, security fences to protect the territories from illegal immigration.

Britain's ban on the right of sentenced **prisoners to vote** has been ruled unlawful by the European Court of Human Rights. The ruling will have a direct impact on seven other European countries with a similar ban.

Bombs in paradise

A series of three bomb blasts killed 19 people, as well as three suicide-bombers, in **Bali**. This was the second attack in three years: 202 people were killed in a much bigger attack in October 2002. See article

India and **Pakistan** set a deadline of January for an agreement to end their confrontation on the Siachen glacier, the world's highest conflict.

Pakistan said it had arrested Latifullah Hakimi, a leading spokesman for the Taliban.

A fresh round of talks between **China** and **Japan** tried and failed to end a stand-off over drilling for gas in the East China Sea. See article

Hoping to put it behind them

Reuters

Algerians voted by a large majority, according to (disputed) official figures, to endorse a Charter on Peace and National Reconciliation. This was intended to draw a line under the civil strife that ensued, leaving some 150,000 dead, after the army stepped in when Islamists won the first round of a general election in 1991. The charter offers an amnesty to all but those guilty of the worst crimes but would, say critics, give the army impunity for past misdeeds. See article

The **Palestinians'** main secular party, Fatah, which has been struggling to impose its authority, did better than expected in the third of four rounds of local elections, winning around 54% of the seats, while the Islamists of Hamas got 26%. But the poll in the Gaza strip, where Hamas is strong, was put off. See article

Giving in to pressure from western governments and the UN, **Iraq's** government reversed a dubious decision that would have made it virtually impossible for Sunni Arabs and other opponents of the country's draft constitution to block it in a referendum due on October 15th. See article

Anonymous British officials accused **Iran** of helping Shia militias in southern Iraq to attack British forces there.

The breakaway state of **Somaliland** held its first multi-party general election since it seceded from anarchic Somalia, of which it is still legally a part, more than a decade ago. All three competing parties want independence.

Counsel for the defence

George Bush nominated Harriet Miers to fill the vacancy on the **Supreme Court**. The choice of a White House lawyer surprised many conservative activists who moaned that Mr Bush had thrown away an opportunity to reshape the court. Meanwhile, John Roberts began his new job as chief justice of the United States. See article

A former marine who worked in the **vice-president's office** for both Al Gore and Dick Cheney is being investigated for passing information to the Philippines' government.

In a snub to the White House, the Senate voted by 90-9 to set tougher limits on how American troops can **interrogate terrorist suspects**.

Two more indictments were brought against **Tom DeLay**, this time for money-laundering political funds. Mr DeLay, who stepped down as the Republican's majority leader in the House of Representatives last week, called the new charges “an abomination of justice”. See article

Judith Miller, a *New York Times* journalist who was imprisoned in July for refusing to testify about her sources, was released from jail and testified to a grand jury investigating the leaking of Valerie Plame's identity as a CIA agent.

An investigation began into the **capsizing of a tour boat** on Lake George in New York state's

Adirondack mountains; 20 elderly passengers were killed.

Weather report

At least 160 people were killed after **Hurricane Stan**, carrying winds of up to 80mph, ploughed through Central America causing landslides and flooding and forcing thousands to flee their homes. El Salvador (already shaken by the eruption of its biggest volcano) and Guatemala were the worst affected and struggled to help those most at risk.

Alberto Fujimori, **Peru's** former president who was ousted from power five years ago, announced he would run for the presidency next spring. He did not say whether he would return to Peru, where he faces arrest on charges of human-rights abuse and corruption, or fight the contest from Japan where he lives in self-imposed exile.

The United States reported that a record 464 people had died trying to cross the border from **Mexico** in the year ending September 30th, a 43% increase on the previous year. See article

Getty Images

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Business this week

Oct 6th 2005
From The Economist print edition

Chocks away

The board of **Airbus's** parent company, EADS, approved the launch of its new mid-sized aircraft, the A350. But the company will not proceed to draw down launch aid promised by European governments while it hopes for a bilateral settlement of the trade row with America over such subsidies.

NTL, a British cable operator, confirmed it was buying **Telewest**, a rival, in a deal worth £3.4 billion ($6 billion). The move creates a "triple play" provider (phones, TV and broadband) in Britain's telecoms market that will provide competition to both BT (phones and broadband) and BSkyB (TV).

A subsidiary of Sprint Nextel, America's third-biggest telecoms firm, filed a lawsuit against Vonage and Voiceglo Holdings claiming that the companies had infringed Sprint's patents relating to **voice over internet protocol** technology. Both Vonage and Voiceglo offer services that enable calls over the internet.

Google and **Sun Microsystems** threw down a challenge to **Microsoft** by agreeing jointly to "promote and distribute" their technologies. As a start, Sun will incorporate Google's toolbar into its Java packages, but techies were more excited by the potential for collaboration on OpenOffice, an alternative to Microsoft's Office software.

Electronic firms that back the **Blu-ray** technology for high-resolution DVDs, notably Sony, received a boost when **Paramount Home Entertainment** said it would also support the format in addition to supporting **HD-DVD**, a rival and incompatible format. Last week, HD-DVD had received a boost when Intel and Microsoft said they would be supporting it, not Blu-ray.

Putting on the brakes

Ford and **General Motors** reported sharp falls in vehicle sales for September. Ford's overall sales fell by 20%, compared with September 2004, and GM's by 24%. Sales of light trucks, which include sport-utility vehicles, shrank by even more as consumers fretted about petrol prices. Meanwhile, GM said it was selling its 20% stake in **Fuji Heavy Industries**, a Japanese carmaker. **Toyota**, which reported its best-ever quarterly sales in America, will buy almost half of GM's stake.

Boots, a British health and beauty retailer, said it intended to merge with **Alliance UniChem**, a pharmaceutical retailer and distributor. The new company will have a market capitalisation of around £7 billion ($12 billion). Boots wants to refocus its business, but most analysts think the merger comes too late for the icon of the British high street to challenge the fierce competition it has encountered from supermarkets. See article

Parmalat is laying another claim against a large financial institution for allegedly contributing to its collapse in 2003. It will sue **Credit Suisse First Boston** for *euro*7.1 billion ($8.5 billion). The trial of the Italian dairy firm's founder and 15 others on fraud charges connected to the *euro*14 billion bankruptcy began last week, only to be adjourned until December. This week, Parmalat also began trading on Milan's stockmarket again after it had relisted.

The great game continues

Kazakhstan's government said it would seek “strategic control” of **PetroKazakhstan's** assets in the country, despite its imminent takeover by **China National Petroleum Corporation**. PetroKazakhstan's shareholders (the company is listed in Canada) are due to approve the $4.2 billion deal on October 18th. Meanwhile, **Lukoil**, Russia's biggest oil company, confirmed that it is close to buying **Nelson Resources**, another Canadian-listed firm that maintains energy assets in Kazakhstan, for $2 billion.

NRG Energy, based in New Jersey, said it would buy **Texas Genco**, an electricity wholesaler in the Houston area, for $5.8 billion. See article

BP issued an assessment on the effects of Hurricanes Katrina and Rita to its business, the first big oil company to do so. The storms swept away $700m in profit for the third quarter and caused the loss of 145,000 barrels a day in oil production—more than analysts had thought. Separately, the Insurance Services Office, a firm that provides data to the insurance industry, estimated that 1.6m American policy-holders would file claims, stemming from Katrina, that would total $34.4 billion.

Conflicted?

The Institute for Supply Management's **index of business activity** in America's services sector fell to 53.3 in September, far below Wall Street's expectations, reflecting concerns over the impact of rising energy costs and the recent hurricanes. However, the ISM's manufacturing index beat forecasts and rose by six points to 59.4. The optimism is fuelled by reconstruction prospects in the Gulf coast region.

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The sun also rises

Oct 6th 2005
From The Economist print edition

Japan's chances of prosperity and influence look surprisingly bright

IT HAS taken an extraordinarily long time, but Japan really is now recovering from its debt- and deflation-ridden stagnation of the past 15 years. Proper jobs are being created, wages are rising and economists are raising their forecasts of economic growth—all despite worries about high oil prices and an American slowdown. The prime minister, Junichiro Koizumi, grabbed the world's attention last month by calling and winning a snap general election, as a referendum on economic reform. Foreign investors are rushing to Tokyo so as not to miss the fun. There is a spring in the step of Japanese politicians and diplomats, relieved that they no longer have to apologise for Japan's weakness, pleased that they might now be better placed to deal with those bumptious Chinese. They have to pinch themselves to be sure it isn't all a dream.

In a way, it is. The turnaround in perceptions of Japan has been so sudden that it risks being overdone. The immediate road ahead for the economy still looks bumpy, with prices continuing to fall, albeit slowly, overall lending contracting and a big budget deficit of 6.4% of GDP making tax rises look probable. With their wages rising and jobs feeling more secure, consumers may soon start to spend more, allowing economic growth to be led by domestic demand rather than by exports and capital investment. But that process too is likely to be gradual, as households may well also rebuild their savings, which have been depleted during the past decade.

Gloomy old hands then turn to the longer term to prove that after autumnal optimism will come winter. Japan's population is starting to shrink, and so is its labour force. With productivity growth meagre in recent years, that implies a bleak future: the OECD recently calculated the country's potential growth rate till 2010 at a mere 1.3% a year. Mr Koizumi is a radical only by Japanese standards, and his party rules give him but one more year in power. And China, surely, is the real star of Asia, destined to out-sprint the sluggish, over-rigid Japanese and eventually to dominate the region's politics as well as its economy.

Japanese tortoises

In the short term, it is right to be cautious. Japan's immediate prospects matter greatly for a

world worried about slowdowns elsewhere, and forever depressed about reform and recovery in the other great has-been economy, Germany. But, better though they look, they could be prey to both external shocks and the vagaries of the economic cycle. The longer term is much more important, for both economic and political reasons. If the world's second-biggest economy is doomed to a genteel decline, then East Asia in future will have one great economic power rather than two and no one to balance China's rise except India, way over to the west, or an over-extended America, across the ocean.

Yet Japan is not doomed to decline. The slow and steady really do win races, and not just in fables. As our survey in this issue argues, Japan has been going through a long wave of incremental reforms, which together have changed politics, the economy and financial markets far more than most people realise, promising the country a bright long-term future. September's election result confirmed that that process is now accepted and that it will continue, with a steady slimming of the state's role in the economy. Until the corporate debt burden had been shed, and until deflation has ended, those reforms always looked beside the point, too weak to counter the ever-present risk of economic meltdown. With that risk gone, the pile of incremental reforms now has a chance to make a difference. And the crucial difference they will make is to the incentives governing corporate, political and financial behaviour.

Chinese hares

The slow growth in productivity that makes OECD forecasters gloomy about Japan's potential was a consequence of the country's astonishing waste of capital during the 1990s, combined with a reluctance to cut jobs. Money was misallocated during the great stock and property bubble of the 1980s, but then even more was wasted in the next decade, as banks kept “zombie” companies alive and politicians raided the biggest pork barrel in history. Now that is past, even a modest improvement in the allocation of capital and the use of labour would boost returns and productivity. Reforms in corporate law and changes in the capital markets make it likely that the improvement will be better than modest. And, as workers become scarce again, further investment in information technology and other sorts of automation should boost productivity.

The ageing and shrinking of Japan's population over the next 10-15 years could thus raise productivity, not reduce it. With labour short, sentiment and social concern will not impede efficiency, as they did in the over-manned 1990s. And the strengths that made Japan rich in the 1970s and 1980s—good education, advanced technology and smooth co-ordination within companies—will again come to the fore.

There is plenty more to be done if Japan is to achieve this brighter, high-productivity future. Pension and health costs need to be cut; Japan's universities need to be revamped; antitrust policy needs to be reinforced in order to foster more competition. Above all, the politicians need to avoid messing up macroeconomic policy by raising taxes too sharply.

If all that is done, however, great prizes are within reach: rising productivity, rising living standards, a rising international reputation and, above all, a rising chance to face up to China on equal, or even superior, terms. Japan's relationship with China is a scratchy, tense affair; the latest dispute concerns gas and gunboats (see article). If conflict—diplomatic or military—is to be avoided, Japan needs to become stronger, but also to foster other Asian alliances, perhaps through European-style regional institutions. To its Asian neighbours, the Chinese hare is impressive but also worrying. A Japan that showed itself to be a steady, prosperous and reliable tortoise would be an appealing counterweight. In Japanese fables tortoises do win races, but they are also something else: they are symbols of potency.

Economist.com OPINION

Pickled ideologues

Bury Lenin

Oct 6th 2005
From The Economist print edition

MEPL

Vladimir Putin should evict his neighbour

“WHY do you want to see this monster?” Russians sometimes ask the visitors who queue at the entrance to Red Square, waiting to go through the metal detectors, past the smoking guards and into the Aztec-style mausoleum. Hats off and hands out of pockets, tourists peer at the corpse in the flatteringly dim light, before being directed along the Kremlin wall, where other Soviet luminaries are interred. Now there is talk that Russia should put an end to this ghoulish thrill and, finally, bury Lenin.

The idea of evicting Lenin from Red Square—where he has reposed since his death in 1924, except for a brief wartime evacuation to the Urals—was first mooted even before the Soviet state he founded collapsed. In the 1990s, Boris Yeltsin intermittently used this Bolshevik mummy as a prop in his tussle with the communists. There was talk of a referendum to determine Lenin's fate, but in the end Mr Yeltsin managed only to deprive him of his honour guard. The issue has arisen again partly because an exiled White Russian general was this week reverentially reburied in Moscow, and partly because one of Vladimir Putin's top officials has said it is time for Lenin to go.

Two sorts of people would suffer if he does. One is his embalmers (who have to do frequent maintenance work but are rumoured to supplement their income by pickling mafiosi). The second, bigger, group is Russia's communists. The mausoleum is still the focal point of their demonstrations, though to reach it they now have to march past the luxury car showrooms around

the square. Disturbing him would still carry some risk: regrettably, the communists still provide the most meaningful parliamentary opposition. So Lenin has so far been left alone. To remove him, Mr Putin once said, would be to tell people who once espoused his ideas “that they had worshipped false values, that their lives were lived in vain”.

Unfortunately, they did worship false values. Lenin, it is often said, was not as bad as Stalin, a companion in the mausoleum until Khrushchev unceremoniously ejected him. Perhaps; but Lenin was still a ruthless fanatic, who helped to plunge his country into civil war and to blight its history and those of many of the countries around it. More important, Lenin's legacy haunts Russia still.

Mr Putin may have many faults, yet (despite his revival of communist symbols and the old national anthem) he is no Soviet dictator. Some of his policies, however, bear traces of the old ideology. Russian foreign policy is still warped by the phantom pain of its lost empire. The government still has too little regard for private property, too often shows a reflexive suspicion of business, and has an inflated idea of the state's proper role in the economy—as recent developments in Russia's energy sector demonstrate (see article).

The best case for leaving Lenin on display is that he is a big and terrible part of Russia's history. Rewriting history was a Bolshevik speciality; Russia's failure to acknowledge its past is at the root of many of its problems. But that is an argument for museums and school text books, not for keeping a corpse in the heart of the capital city. Lenin had to be tactfully covered up when George Bush and others visited for the second-world-war commemorations in May and, as the occasional angry questions in Red Square demonstrate, his presence irks many Russians. Let him be laid to rest in St Petersburg, like the tsar the Bolsheviks murdered. Russia needs to remember its past, but also to bury it.

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Terrorism

The bomber will always get through

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AP

But, in South-East Asia, he is not winning

ONCE again, a balmy Bali night has been ripped apart by bombs, aimed at innocent foreign holidaymakers though mostly killing innocent Indonesians. Once again come the familiar fears: can the war on terror ever be won? Is Indonesia a safe place for foreigners and their vital investments? Indeed, can a country as poor and fragile as Indonesia be sure of surviving such efforts at destabilisation and still remain secular? Or is it fated to fall like a domino, the first piece in the construction of an Islamic caliphate in South-East Asia? That is the avowed aim of Jemaah Islamiah, the al-Qaeda associate that is suspected of exploding the three bombs that killed 19 people—along with three suicide bombers—on October 1st.

This latest outrage may have succeeded in reminding the world of the region's vulnerability, but its perpetrators are losing. The caliphate was always a crazy vision, and the bombers are failing to achieve even their more modest ambitions. Since they killed 202 people in Bali in October 2002, they have repeatedly tried to mount spectacular follow-ups, but with only limited success. In September last year, they tried to hit the Australian embassy in Jakarta, but inflicted only moderate damage, and instead of killing Australian diplomats, killed Indonesian embassy workers and passers-by.

Thanks to some excellent police-work by Indonesia itself, and to the close co-operation among the countries of South-East Asia and with others such as America and Australia, Jemaah Islamiah is a weaker force than it once was. Its spiritual leader, Abu Bakar Basyir, is behind bars, as are many of the organisation's operatives, most notably Hambali, allegedly the group's operations chief. At least two ring-leaders remain at large, however—including the man said to be the group's bomb-maker. And that is more than enough to cause occasional mayhem.

The latest blasts were apparently caused by small and simple devices (see article), unlike the huge

ammonium-nitrate bomb used in 2002—perhaps a sign that the bomb-makers' supply-chain is being disrupted. And the bombers blew up only the softest of soft targets. Such suicide attacks are impossible ever to eliminate entirely, as other countries have learned to their cost, but the damage they can inflict is limited.

Elsewhere in South-East Asia, the war against the terrorists seems to have been more successful. Australia, Singapore and Malaysia have all been menaced, but none has yet been hit. Some terrorist violence continues in Thailand and the Philippines, but it takes the form of localised civil war. In neither case is the stability or survival of the government remotely threatened. The “caliphate” established so far extends to a few jungly pockets in Mindanao, in the southern Philippines, which are controlled by bandit outfits that may be very loosely linked to Jemaah Islamiah or al-Qaeda.

If the caliphate is an unrealisable dream, what do terrorists in South-East Asia seek to achieve? One purpose of terror is to force governments into repressive measures, which alienate people and then, supposedly, generate support for causes the terrorists espouse. There is not much sign of this happening anywhere in South-East Asia, with the exception of the hamfisted response of the Thai government to its separatist movement. The constraints of democracy have mostly kept the response to terror proportionate. In Malaysia, under the government of Mahathir Mohamad, anti-terror laws were indeed abused and amounted to a crack-down on the legitimate opposition. Yet Dr Mahathir's ratings suffered for this. His successor is being a bit less repressive, making far fewer arrests, though still holding in jail people he shouldn't.

Won't win, can't win

Another of the aims of terrorism is to inflict economic damage, so weakening the target government. Yet there is little sign of this happening either. All of South-East Asia's economies, even that of the Philippines, are more or less booming, growing at 4% a year or better. Indonesia's grew by 5.2% in the second quarter of this year. The most the terrorists can hope for is to hurt the notoriously nervy tourist trade (though after the first Bali bomb, tourists speedily returned). But tourism is only about 5% of Indonesia's economy, a lower figure than for most other countries in the region.

After its attempt to assassinate Britain's prime minister, Margaret Thatcher, and her entire cabinet at the Conservative Party conference in Brighton 21 years ago, the Irish Republican Army declared: “Today we were unlucky. But remember, we only have to be lucky once. You will have to be lucky always.” Chilling, but untrue. Terrorists will always manage to kill people, if they are cunning enough or pick easy enough targets. Indonesia will, perhaps, never be entirely free of them. But for the terrorists that is a far cry from victory.

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Economist.com OPINION

Turkey and the European Union

Now make Turkey's case

Oct 6th 2005
From The Economist print edition

AFP

On being European and different

Get article background

AFTER two days and a night of unseemly horse-trading between Turks, Austrians and other Europeans, Britain's foreign secretary, Jack Straw, made bold claims for the deal he brokered this week. The start of entry talks between the European Union and Turkey, he said, marked an “historic day for Europe and the whole of the international community”.

His bleary-eyed triumphalism may yet prove premature. But the reverse of what he said is certainly true. It would have been an historic disaster if, 42 years after promising the Turks the possibility of entry, and ten months after giving a definite date for talks to begin, the Union had slammed the door in Turkey's face. That outcome would have been dreadful, both in its direct consequences and because of the opportunities lost.

Among the short-term results, Turkey's impressive but still fragile programme of economic and political reform could have slowed or worse. Those Turks—starting with Recep Tayyip Erdogan, the prime minister—who have invested in a European future would have been left horribly exposed. Worse, Muslims in Turkey and elsewhere would have concluded that Europeans bore a grudge against them because of their faith alone. This would have encouraged all those, from Osama bin Laden to the western world's religious far-right, who long for a clash between Islam and the historically Christian world.

It is also true that a chance now exists to achieve something vastly desirable. All sides will benefit hugely if what is best in Europe, including its tolerant, liberal-democratic tradition, can finally come together with what is best in Turkey—including the dynamism of a demographically young

nation that makes Europe's heartland seem sluggish by comparison.

But reaching that goal will require hard work and political courage. It will also need a prudent openness to the possibility that somewhere in the process, one or other party (and it could well be the Turkish side) will conclude that the price is too high. That would be disappointing but not necessarily terrible—as long as the EU expects of Turkey only the same as it would of any other applicant.

In Turkey, people's enthusiasm for a European future has already waned in the face of the "rudeness" of potential partners such as France and Austria. How can it be, many Turks ask, that people in those countries do not see the obvious benefits of having them as members? If the Turks are to find their way to Europe, they will need to grow thicker skins.

For European politicians, the queasiness of many citizens about embracing another large, impoverished country is a hard, irreducible fact. In several European countries, far-right parties are doing well by playing on fears of Muslim immigration. The response of the EU's leaders to these realities may yet be statesmanlike, or opportunistic. But it is politics, not technicalities, that will finally decide Turkey's fate.

And the politics will be tough. All the arguments against incorporating the Turks seem obvious and, to some politicians, tempting. The case for keeping the doors open has to be reasoned through more carefully. The onus is on politicians to convince voters that making western Europe a sort of up-market gated community would be worse than useless: it would not protect existing job-holders, or keep desperate labour migrants out, or stem Europe's relative decline in the world economy. If politicians are responsible, they will also point out that trying to toughen the rules unreasonably for Turkey will not make that country go away, or reduce its importance, or slow the pace at which it is changing: it will simply increase the chances that Turkey will evolve in an unhappy direction, towards Muslim fundamentalism or militaristic nationalism.

The right sort of scepticism

At the same time, politicians should accept that one ground for Turco-scepticism is, in its own terms, perfectly sound. To the delight of some and the dismay of others, Turkey's presence will make it harder for any country or axis to play a dominant role in Europe. With 15% of the total population, the Turks will hardly take over the Union themselves; but their membership will deny preponderance to others.

So France's ex-president, Valéry Giscard d'Estaing, is right to say that an EU including Turkey will be a looser grouping than some people desire. The Turks may well wreck things for any state or pair of states which still hope the EU as a whole will act as a mouthpiece for their own political, or geopolitical, ideas; or that the Union will turn into a super-state with one or two of its current members in charge.

But in fact, those dreams have been dashed already, and it was not the Turks, or even the party-pooping Brits, who destroyed them. Among the many messages delivered by French and Dutch voters when they rejected the Euro-constitution, one was certainly this: that there are still some fundamental questions—such as how to mix efficiency with fairness, or tolerance with responsibility—that cannot be settled by pan-European edict alone. And many would rather see a somewhat looser EU than have choices they abhor imposed on them from above.

So as politicians consider the arguments in favour of embracing Turkey, they might try this one: the Turks' aspiration to be "European but different" may yet give heart to people in other parts of the EU who are willing to participate in the Union, and abide by commonly-agreed rules, but not to

sacrifice their own nations' distinctiveness. Such people are quite numerous, and Europe is the stronger for it.

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Economist.com OPINION

Internet governance

America rules OK

Oct 6th 2005
From The Economist print edition

Plans for global management of the internet are a threat to its future

WHY should America control the internet? A growing number of governments are asking this apparently reasonable question. At a diplomatic meeting last week in Geneva, the European Union unexpectedly dropped its support for the current arrangement, and sided with America's critics (see article). America could now find itself isolated as negotiations over future regulation of the internet continue.

The critics' point of view seems quite understandable. The internet is not just a hugely important tool of global communication but also an engine of economic growth. Other countries quite understandably balk at American hegemony over something that matters so much to their future. Yet although America's exercise of power in the bricks-and-mortar world may not always have been flawless, its oversight of the internet, which it invented (Tim Berners-Lee, a Briton, is sometimes credited with the feat, but he created the world wide web) has been remarkably benign. That's probably partly because politics has been kept out of it. The longer it stays that way, the better.

Benign neglect

Most people think of the internet as decentralised and thus uncontrollable. That's largely true; nevertheless, its infrastructure requires some co-ordination, so it needs a bit of governance. This is currently done by a non-profit group called the Internet Corporation for Assigned Names and Numbers (ICANN). This organisation operates under a contract from the American government, and consults private-sector firms and groups of techies and users.

Much of ICANN's work is boringly technical. It co-ordinates such features as domain names (like .com or .net), routing numbers and technical standards. But small technical details can sometimes have big political ramifications, and ICANN has often found itself embroiled in

controversy. For example, many countries were outraged when ICANN considered creating a .xxx domain name for pornographic websites. (It diplomatically put the idea on hold.)

Nevertheless, ICANN's stewardship has succeeded because its focus has been not on politics, but on making the network as efficient as possible. The sometimes fierce debates that break out among techies have been conducted transparently. The result has been an internet open to innovation and free expression, led mostly by the private sector and relatively free from government interference.

Yet because the system runs under American auspices, other countries are unhappy with this arrangement. Many of those who want to relieve America of its control think ICANN's job should be taken over by a United Nations agency.

To anybody who has spent much time observing the UN at work, this sounds like a poor idea. It is no accident that the world's telephone systems remained so expensive and static for so long. They have been heavily regulated nationally and their international links have been controlled by the International Telecommunication Union, a UN body which once rejected the idea of the internet in favour of a more controllable and less efficient system. That standard never amounted to much. The ITU's approach reflected the interests of state-run telecom monopolies, which themselves are now being shaken to their foundations by the internet.

It is also no accident that many of the countries loudest in their demands for the internet to be taken out of American hands are those, such as China, Iran and Saudi Arabia, that are keenest on restricting its use by their own citizens. These and many other countries are hoping to use the lead-up to the UN's World Summit on the Information Society to begin to wrest control away from America. By changing its position last week the EU had hoped to act as a “bridge” between America and other countries. Instead, it has simply isolated America, with potentially damaging results.

America has offered olive branches to its critics. This summer, it acknowledged that other countries have sovereignty over their national addresses, and said it would never disrupt the system (ie, kick France's .fr address offline). And, at the meeting last week in Geneva, it supported the idea of a forum in which all governments can discuss these matters in an “evolutionary process”. That sounds like an excellent scheme: just as startling as the speed of technological development is the slowness of decision-making in international forums. If this move works, it should succeed in parking the issue harmlessly for many years.

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Illegal immigration

Decapitating the snakeheads

Oct 6th 2005
From The Economist print edition

AP

How governments could beat the people-smugglers at their own game

IN AMERICA, they are called “coyotes”; in China, “snakeheads”. Whether they be wild dogs or serpents, people-smugglers are a thriving species with no shortage of prey. They herd Mexican hopefuls over the parched expanses of the Arizona desert; they pack Chinese immigrants into airless crates on transpacific container ships; and they ferry Africans across the Mediterranean, evading Italian coastal patrols. Thanks in part to their efforts, up to 350,000 illegal immigrants steal across America's border from Mexico each year, and as many as 800,000 enter the European Union.

This week the Global Commission on International Migration, set up in 2003 by Kofi Annan, secretary-general of the United Nations, delivered its report on the movement of people around the world (see article). The 19 worthies on the commission, drawn fairly evenly from countries that import and export labour, roundly condemned illegal immigration. The illicit flow of people across borders is a challenge to a country's sovereignty, they concluded, and gives migration in general a bad name. It is also dangerous for the immigrants themselves. Last year a record 464 people died crossing from Mexico into America, and each year around 2,000 people drown in the Mediterranean on their way from Africa to Europe.

Damaging and dangerous it may be, but illegal immigration is also good business. Smugglers rake in around €4 billion ($4.7 billion) a year from the EU alone, reckons Michael Jandl, of the International Centre for Migration Policy Development, an intergovernmental think-tank, based in Vienna. Smugglers charge €3,000-8,000 to convey people from Pakistan to Europe. But that is not all they can do. They will fix a British marriage for £5,000 ($8,800); and falsify an Italian residence permit for €4,500. Some outfits even offer warranties (if the first attempt to cross the border fails, the second one is free) and money-back guarantees. Smuggling, Mr Jandl says, has evolved into a sophisticated service industry. He has an intriguing idea of how to defeat it.

The best way to do this, he argues, is not just to ban it, but also to undercut it. Governments, he suggests, should sell temporary, two- or three-year visas in the smugglers' best markets. The visas should be priced to compete with the smugglers' rates. One-third of the visa fee could be returned to immigrants when they depart the country, and anyone who had bought a visa in the past would be free to buy another one, provided they did not break the rules. These features would be powerful incentives not to overstay. Some fraction of the fee could also be refunded to immigrants who pay social-security taxes, giving them a reason to keep out of the underground economy.

The new visas need not increase immigration rates overall, Mr Jandl insists. Rather, they aim to muscle in on the smugglers' market share, steal their best customers, and snatch their illicit profits. Smugglers might slash their prices to compete. But a successful smuggling ring can be a costly undertaking. And if governments invest in tighter border controls and better fraud detection they can push smugglers' costs up, even as they drive demand down.

Put it to the test

Would it work? The demand for legal permits is a big unknown. There are probably many law-abiding people willing to pay for a legitimate visa who would never pay a smuggler. The price Mr Jandl takes as his benchmark—the smuggler's fee—does not reflect this latent demand. On the most controversial border of all, between the United States and Mexico, Mr Jandl's scheme might attract far more custom than it could possibly handle. The price of the visa could of course be raised to keep sales down to whatever level the government desires (or, Mr Jandl says, a cap on the number of visas could be introduced). But high prices or strict rationing would push more people back into the arms of the smuggling industry.

Many of the questions raised by the scheme can be answered only by trying it. Mr Jandl suggests a small pilot effort between the EU and a country such as Albania. Whatever the results, the spirit of the proposal and others like it is commendable. Border crackdowns and mass deportations have populist appeal, but they are clumsy, costly and cruel. Mr Jandl's proposal relies on economic logic, not bureaucratic brawn. At the very least, it would make the snakeheads hiss and the coyotes howl.

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On VOIP and broadband, stagnation, Kamchatka, higher education, Alberta, eminent domain, Hurricane Katrina

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Cheap talk?

SIR – Rather than "voice over internet protocol", the disruptive element in the telecommunications business right now is the spread of broadband connectivity ("How the internet killed the phone business", September 17th). VOIP, and a host of other new services, depend on broadband for their existence. We are providing television, music downloads, video-on-demand and video calls, with VOIP as an add-on commodity offered at tariffs comparable to those of Skype.

Moreover, VOIP will have a more limited impact in Europe than America because of the different mix of telephone traffic. In America, long-distance calls, where VOIP has its greatest potential, represent the lion's share of traffic, while in Europe it is predominantly fixed-to-mobile and local. On the latter, the effects of VOIP (understood as free voice telephony) are limited because fixed-to-mobile involves a termination fee and local calls are already very cheap and offered in all-inclusive flat-fee packages. By 2010, VOIP will account for 9% of the Italian market and only about 3% of total revenues. It will be roughly the same in Britain and slightly higher, around 4%, in France and Germany. Yes, the elephants are dancing, as you put it, but to the tune of broadband.

Riccardo Ruggiero
Chief executive officer
Telecom Italia
Milan

Europe's next degeneration

SIR – Charlemagne claims that Germany's reform gridlock is a presage to gridlock in the European Union and concludes that, for the time being, "a genteel but depressing process of stagnation" is here to stay (September 24th). To wit, Europeans want myriad cobwebs to be removed, but not just yet—reform can wait just a little bit longer. But Charlemagne puts too much hope in "reform", whenever or however it may come to pass. Europeans know very well that Americans and Asians work way too much for their taste. And they know even better that stagnation does not have to be all that depressing. In fact, it can be not only genteel but a lot of fun too. As ever, the model is Venice in decline, which has been the most cheerful place on the planet for three whole centuries.

Ranko Bon
Motovun, Croatia

Crap towns

SIR – Having thoroughly enjoyed a trekking holiday (complete with bears) in Kamchatka, I would contend that its main city, Petropavlovsk-Kamchatsky, though undeniably Soviet in appearance, is rather less “hideous” and decidedly more charming than, say, Luton or Middlesbrough (“Big bears and other extremes”, September 24th).

Rory Harden
London

Reform syllabus

SIR – Your survey of higher education provides an interesting, if somewhat misleading, overview of the situation in Europe (September 10th). While appropriate funding levels and autonomy are preconditions for the successful reform of European universities, the efforts of constructing a European higher-education area has not come “too little, too late”. The current reforms involve the higher-education community and governments in 45 countries and constitute the most sweeping changes to higher-education systems in Europe for centuries. More than just introducing “comparable qualifications and transferable credits”, this process is transforming how higher education deals with issues of institutional governance, research and education, quality assurance, mobility and the relationship with external stakeholders. With the commitment that universities are showing to these reforms, the outcome will lead to stronger institutions that are better suited to meet the needs of European society and to contribute to the project of creating a competitive European knowledge society.

Lesley Wilson
European University Association
Brussels

Savings for a rainy day

SIR – Your reference to Alberta's contingency fund as “stuffed with C$12 billion” is off the mark (“The good times roll”, September 10th). In fact, not a dime has been added to the Heritage Fund since 1987. In the intervening years, the entire yield has been diverted to general revenues and inflation has eaten away at the capital base. Alberta has but C$12 billion for 3m citizens; this is puny in comparison with Alaska's fund of about $30 billion for only 600,000 citizens.

Allan Warrack
Professor of business emeritus
University of Alberta
Edmonton, Canada

Redeveloping Ardmore

SIR – Your article on eminent domain contained inaccuracies about the redevelopment process in Ardmore, a part of Lower Merion, Pennsylvania (“Hands off our homes”, August 20th). Foremost, at no time did the Township of Lower Merion's communication to business owners “inform them that their shops were to be demolished”, nor were they told “they would have to move”. The Township's initial letter last year notified eight businesses in the proposed redevelopment area of the Township's intention to appraise certain properties for potential future acquisition. It was made clear the Township would fully assist with relocation, preferably in Ardmore, should this proposal move forward.

Moreover, establishing a part of Ardmore as a redevelopment area came after a lengthy and inclusive process involving extensive input from business, civic leaders and residents. The local

business-district association representing 300 local businesses has been supportive of the plans. Within the redevelopment area, many businesses are struggling with falling sales concomitant with a district in decline. The Township has yet to issue requests for proposals for redevelopment projects in Ardmore; only when developers' proposals are received will important decisions be made for the revitalisation of Ardmore that could affect business owners.

Matthew Comisky
Board of Commissioners
Lower Merion, Pennsylvania

Civics 101

SIR – For your American readers who felt the government should have no role in the aftermath of Hurricane Katrina, let me quote this mission statement: “We the people of the United States, in order to form a more perfect union, establish justice, insure domestic tranquillity, provide for the common defence, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity, do ordain and establish this constitution for the United States of America” (Letters, September 24th).

Rainer Schoenrank
San Francisco

SIR – In the past 100 years, the American government has lifted its people out of the Great Depression, made crucial contributions to victory in two world wars, heavily influenced the fall of communism in Europe, and landed men on the moon to boot. Seemingly the train moves just fine if only it has the right engineer.

Erik Goodman
Dayton, Ohio

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The Everglades

Water, bird and man

Oct 6th 2005 | HOMESTEAD AND WEST PALM BEACH, FLORIDA
From The Economist print edition

Still Pictures

A vast environmental project in Florida with lessons for the post-Katrina clean-up

AT ITS south-east corner, America peters out into something that is neither land nor sea, but a subtropical swamp in between. The Indians who hid in this inaccessible place called it the Pa-hay-Okee, the grassy river. “The blowing gray-gold flow of sawgrass in the glittering fresh [glades],” wrote Peter Matthiessen, a naturalist and novelist, “stretched away forever, north and south, to the mysterious dark hammock isles on the horizon.”

This is the Everglades, a place once so rich in wildlife that America's greatest bird painter, John James Audubon, described the sun blotted out for minutes at a time by the great flocks of herons and egrets flying past. Now, the Everglades is the site of America's largest civil-engineering project and the world's most expensive environmental clean-up. But this, too, is in danger of petering out into a swamp—one made up of conflicting interests, state ambition and federal indifference.

Restoring the Everglades matters for its own sake. But it also matters because, after Hurricane Katrina, the balance between protecting people from nature, and protecting nature from people, has become an urgent matter of public policy–and this is the place where that policy has been most exhaustively thrashed out. As in New Orleans, the Everglades saw a disastrous flood (in 1928) when a levee broke and thousands died. As in the Everglades, the Louisiana bayou could not absorb the storm surge in part because its natural environment had been degraded by flood-control measures and housing, and could no longer act like a sponge.

The Everglades project is a test of whether it is possible to restore a whole ecosystem, while still allowing cities to keep on growing nearby. If it succeeds, it will be a model for schemes throughout

the Americas, including the Gulf coast. If it fails, environmental clean-ups will no doubt continue, says Colonel Robert Carpenter, the man in charge of restoration, but they will be too small to do much more than slow the rate of decline.

The whole of south Florida was once one enormous hydrological system, stretching from Orlando to Key West. Abundant rainfall was channelled down the winding Kissimmee river into Lake Okeechobee. From there, water lapped over the southern edge and spread south in a vast curve, moving 100 feet (30 metres) a day, in a sheet flow inches deep but 50 miles (80km) wide. Stands of sawgrass thrived in an imperceptibly undulating landscape of ridges and sloughs, interspersed by teardrop-shaped islands of trees in a pattern that followed the current.

A teeming world depended on the tiny changes of elevation. Snails lay their eggs near the base of the grass stems—too high and the grass topples over from the weight, too low and rising water drowns the eggs. The snail kite feeds on this species, its beak curving precisely into the snail's whorl. Fish ripple out as the water rises and congregate as it falls, providing food for wading birds such as the wood stork.

But in the 1930s, the Army Corps of Engineers (at the behest of the federal and state governments) built a new levee around Lake Okeechobee to dam the southward flood. In the 1940s, it drained the area to the south to create vast sugar fields. In the 1950s, the corps diverted the river, allowing Miami and Fort Lauderdale to grow on the old river bed. In the 1960s, the corps crisscrossed the remnants of the grassy river with dykes, ditches and levees.

The river is now in the wrong place and more akin to a series of ponds. These ponds (called water conservation areas) still have sloping, not flat, bottoms, so the water tilts south, flooding the ponds' southern parts, while leaving the northern bits dry. At the bottom of each pond, the tree islands drown; at the top, they burn: fire and flood at once. Around 60% of the tree islands have been lost; so has the old landscape of ridges and sloughs. With it have gone the tiny changes of elevation, on which the wildlife depended.

About half the old Everglades has been taken for cities or farms. If all the rain that falls on southern Florida were channelled into the remaining half, there would be floods. So 1.7 billion gallons a day is pumped from Lake Okeechobee east and west to the Atlantic ocean and the Gulf of Mexico (where the fresh water duly wrecks the marine environment). And because less water reaches the south of the Everglades National Park, the sea and mangrove swamps are advancing inland at the rate of 12 feet a year.

CERP in the garden of Eden

The old sheet flow has stopped. So the water that remains has to be pumped around in ways that change water levels more abruptly than the vegetation can respond to. Plants that depend on a subtle ebb and flow are dying. The great flocks of waders are gone. Invasive species are appearing, including tropical fish and pythons, which have spectacular fights with the alligators. Underlying everything, argues Tom van Lent, a hydrologist, is a change in the food chain itself. Once it was “primary”: fish ate a mixture of algae and bacteria. Now it is “detrital”: cattails spread everywhere, rotting in the water, and fish feed on the detritus. When something that basic changes, so does everything else. “The ecological system is in a state of near-total collapse,” claims John Marshall, a green activist.

Enter the Comprehensive Everglades Restoration Plan (CERP), which was signed in December 2000, at the last gasp of the Clinton administration. It was expensive ($7.8 billion then, at least $10 billion now), extremely complicated (with 68 projects planned over 30 years) and it demanded a new sort of partnership between state and federal governments, with each side

paying half. But it was also popular: it passed by 85-1 in the Senate and it won the support of virtually everyone: greens and property developers, Republicans and Democrats, sugar farmers and fishermen.

Five years later, not a single CERP project has been built. Costs are rising. The coalition has fractured. And the state-federal partnership is not working. In March, Gary Hardesty, CERP's project manager in Washington, wrote in an internal memo “We have missed almost every milestone. It is different from what we told Congress we would do, and it's not restoration.”

The main restoration idea was simple. More water would be reintroduced into the ecosystem and allowed to flow southwards as it used to. But since CERP could not risk floods, the project was also to improve flood control and water supply in Florida's southern cities.

Everglades restoration was never going to be that simple. Ideally, as much water as possible would be introduced at the top of the system, just below the agricultural area. But that is impossible. The old river of grass flowed in a south-westerly arc, which meant the water flowed slightly faster on the longer, eastern side. This moving wall of water acted as a natural dam: water restraining water. But when the corps moved the river sideways, it destroyed the watery dam. To have let nature take its course would have risked flooding Miami and Fort Lauderdale.

So, instead, CERP is aiming to restart about four-fifths of the old current in the lower half of the system. Water from Lake Okeechobee will be pumped through the upper and middle reaches of the glades in a complicated zig-zag, before being piped back into the lower Everglades. Since this would do nothing to improve the flow in the middle reaches, the plan also calls for removing some of the main dams and canals there. The corps will, for example, punch holes through the L67 canal that cuts across the river, and raise parts of the Tamiami Trail, an east-west road just above the national park. To stop all this “extra” water flooding the system, it has controversial plans to store it above and below ground (more on that in a moment).

The project, in other words, is an attempt to manage the environment back to health. As Bob Johnson, the chief scientist of Everglades National Park, puts it, “it is not a restoration plan as such. It is really an integrated watershed management plan.” That is why it is complicated and costly.

Environmentalists fear a managerial approach is not going to work: the ecosystem is too badly

damaged. Much of the system would benefit, of course, but Mr Johnson points out that restoring four-fifths of the old current might not be enough to save the deeply polluted southern estuaries. So even if it were implemented, CERP would not answer all the problems.

Squabbles over the plumbing

One huge worry is that CERP will be undermined by attempts to satisfy different interest groups: in particular, the environmentalists, who want to save the Everglades, and the town dwellers, who want better flood control and water supply. In the long run, these aims do not necessarily conflict (there is enough water to go round). But they allow for plenty of squabbling. For instance, the Florida Fish and Wildlife Conservation Commission—the hook and bullet crowd—is in charge of the water conservation areas (the "ponds"). Legally, the commission is required to keep these places for hunting, so wants them relatively dry to encourage deer habitat. Environmentalists say these areas were once part of the river bed and need to be drenched again.

Moreover, in a 30-year project, there will always be problems of sequencing: deciding who gets the benefits first. The Everglades National Park—the bit reserved for nature alone—is at the southern end of the system and will benefit last under CERP because, as Colonel Carpenter puts it, the park "is at the bottom and you have to get the plumbing right at the top first."

Given the number of people CERP has to keep happy, squabbles were inevitable. The planners, recognising that this would affect their grand design, adopted something called "adaptive management" as a principle of work (it means that the plan is not set in stone). They also set up a complicated system of consultation. For the first couple of years, this has at least kept the interest groups together. In short, arguments may be inevitable, but do not have to be terminal.

Another worry is that CERP relies too much on untested technology. This particularly applies to how it would store and release the extra water it would add to the ecosystem. The simplest way of doing that would be to buy land and build surface reservoirs. But in southern Florida that would be prohibitively expensive.

Hence, CERP has plans to store the water underground: 1,000 feet down in an aquifer. The plan is to pump billions of gallons down during the wet season and back up again in the dry. This technology is called aquifer storage and recovery (ASR). The system has worked elsewhere and

early tests in the Everglades have shown that you can mix surface and aquifer water without too many ill effects.

But the pressure required to push water down so far is enormous—and could crack the restraining layer of rock round the aquifer. Moreover, there will have to be about 330 ASR wells in the Everglades, making the operation ten times larger than the largest currently in operation (in Nevada). No one knows whether the ASRs will work on that huge scale. A report by the National Academy of Sciences in 2002 doubted it.

So what is the alternative? In about 30 years' time, there may be one. It is almost as mind-boggling as the ASRs. Mining companies are busy excavating limestone pits between the Everglades and Miami to provide construction material. When they are finished (in about 2035), these abandoned quarries will become giant bath-tubs. But, again, they are untested: nobody is sure how much water will leak out.

The vanishing federal partner

The arguments over technology are real, but since even ASR pilot projects have not yet been started, they do not explain why CERP is in such trouble now. The real answer is that the partnership between Florida and the federal government has tilted towards the state. In 2004, CERP was $1 billion over budget and two years behind schedule. Congress failed to authorise money for CERP projects. In the Senate, the sole objector to the project in 2000, James Inhofe of Oklahoma, had become chairman of the committee that governs CERP. And during the debates, the federal government was missing in action.

Florida's governor, Jeb Bush (George's younger brother) took the bull by the horns. He put $1.5 billion of the state's own money towards jump-starting eight CERP projects. It was an act of some boldness. Without the governor, the projects might never have got off the ground. Arguably, Governor Bush saved CERP.

Still Pictures

Disappearing rivers of grass

But he has done so on his own terms and in ways that threaten the original plan. Remember that CERP was a 50:50 federal-state partnership in which the two sides agreed to split the money. The state had agreed to be bound by detailed regulations drawn up by the federal side (an unusual provision in American government). This partnership was a big reason why so many interest groups signed on to the plan,

Mr Bush's plan—dubbed Acceler8—has changed that partnership in two ways. First, the state is spending its own money. In effect, the governor now controls Everglades restoration (it is probably unfair to criticise him for this power grab, given that the federal government was doing practically nothing).

But whatever the rights and wrongs of it, the fact is that Acceler8 has fractured the grand coalition. Shannon Estenoz, a former head of the organisation that brings environmental groups together, says the consensual methods that kept everyone behind CERP have been abandoned. “The public is no longer heard,” says Mr Marshall. Mr Bush responded in kind: he is said to have told aides that “we don't need [the environmentalists'] permission to save the Everglades.”

Second, Acceler8 could upset the balance between environmental and water-supply aims. The state government is hardly indifferent to the Everglades area; after all, Mr Bush has spent $1 billion just on land purchases for reclamation. But its interests are different. The federal government—as steward of the national park—focuses on the environment; the state's main concern is to provide water to the cities and farms of southern Florida.

This is reflected in the water supply plan of the South Florida Water Management District. The state's plan calls for the forecast water needs of cities over the next 50 years to be met by 2010; for farmers' needs to be met by 2015; and for basic environmental standards to be met only after 2020. None of the main environmental aims, such as ensuring a flow of water and boosting water supplies to the national park, appear to be in Acceler8. To the annoyance of Congress, the Florida legislature tore up water-pollution controls (designed to protect the Everglades) to please its powerful sugar lobby. All that raises doubts about how high a priority environmental clean-up has now become.

Greens fear the worst. They believe that when Acceler8 is completed, and the water-supply projects built, the state will abandon CERP, leaving the federal government with a stark choice: either finance the environmental parts itself, or let CERP collapse. That may be scaremongering. But it is already clear that the Everglades project is falling well short of what was first envisaged. A few projects will go ahead, thanks to Governor Bush's intervention—at an unknown cost. Much of the rest of CERP risks falling into limbo.

Stick together, please

And the main reason for the disappointment is one that holds an uncomfortable lesson for New Orleans: you need both the federal and state governments if restoration is to work properly. However awkward it is to have squabbling interest groups, a single, biased paymaster is worse. The implication for Louisiana is that the federal government cannot do everything. The implication for the Everglades is that the federal government needs to do more to keep its share of the original bargain by authorising more projects and providing the cash it promised.

And it needs to do so soon. “Time is running out,” says Bob Smith, a former New Hampshire senator who shepherded CERP through the Senate in 2000. In the past three years, the urban-development boundary that separates Miami from the Everglades has been breached. Three big building projects have also been approved for land that was supposed to be used for CERP and which would, until recently, have been considered off-limits to development. The pressure to build is relentless: Fort Myers and Naples have been America's third and sixth fastest-growing cities over the past 25 years.

This is, says Colonel Carpenter, a once-in-a-lifetime chance to save the remaining Everglades and show that huge clean-ups are possible. Given the relentless land hunger, those who want to save the river of grass probably have about five years in which to restart the comprehensive plan. After that, it may be too late.

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The Supreme Court

The great Miers mystery

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From The Economist print edition

Getty Images

George Bush's new pick for the top court is impossible to read. That may solve an immediate problem for the president, but it poses a challenge for America

Get article background

BESET with allegations that he appoints incompetent cronies to important positions, what does George Bush do? He nominates his former personal lawyer to the Supreme Court. No one is suggesting that Harriet Miers is flat-out incompetent, but is she really the best candidate for a job-for-life on the nation's highest court?

Many of Mr Bush's conservative allies doubt it. “I'm disappointed, depressed and demoralised,” said William Kristol, editor of the *Weekly Standard*, a neo-conservative magazine. “Her qualifications for the Supreme Court are non-existent,” said Patrick Buchanan, a former Republican presidential wannabe. If it were only Democrats accusing the president of letting friendship cloud his judgment, Mr Bush could doubtless shrug it off. But when the *Wall Street Journal*'s first reaction is an op-ed entitled “Cronyism”, and the *National Review*'s website damns with the faintest praise imaginable—“It's not as bad as Caligula putting his horse in the Senate”—surely something is amiss.

Announcing his choice on October 3rd, Mr Bush listed Ms Miers's accomplishments. She currently holds “one of the most important legal positions in the country, the White House counsel”. Her legal career has been long and distinguished: she rose from modest beginnings to become the first woman to lead a large law firm in Texas and the first female president of the State Bar of Texas. She has discharged various public jobs, such as cleaning up a scandal-ridden state lottery commission, with “fairness and integrity”.

All of which is thoroughly admirable and prompted one conservative blogger, Hugh Hewitt, to endorse her as a “solid B-plus pick”. But, as several others pointed out, the Supreme Court is no place for B-plus candidates. Ms Miers has never been a judge, and no one is claiming that her constitutional expertise comes close to matching that of Mr Bush's last pick, the new Chief Justice, John Roberts.

Granted, Mr Roberts was an unusually good candidate. And many voices had argued that in the interest of diversity, the president should pick a woman, a member of an ethnic minority and/or someone from outside the clubby circle of senior judges. Good Supreme Court judges have been found outside this circle before—think of Earl Warren and William Rehnquist. Some would argue that the current court is drawn from too narrow a pool: all its members have been lower-court judges. Wouldn't it be useful for one of the nine to have managed a sizeable firm, as Ms Miers has? Wouldn't that provide, in the words of Thomas Lifson, editor of the *American Thinker* “a necessary and valuable perspective for a Supreme Court justice, one which has sorely been lacking”?

Perhaps. But against that mild plus, there are two colossal question-marks over the nominee. Does she really know enough about the constitution to be one of the nine ultimate arbiters of what it means? And if so, how would she construe it? There is virtually no paper trail for her assessors in the Senate to scan for answers to either question.

Having never been a judge, Ms Miers has made no public judgments. Nor has she given speeches about her legal philosophy, nor penned articles for law journals. She has written plenty of legal advice for Mr Bush, but we can't read it because it is covered by both executive and attorney-client privilege. Mr Bush says she will “strictly apply the constitution...and not legislate from the bench.” Fair enough, but we have only his word for it, and he supplied few other details.

The great Miers mystery troubles both sides of the political spectrum. Liberals fret that the nominee could be more bomb-chuckingly conservative than she appears. Democrats are not nearly as disappointed as Mr Bush's base, however, for they do not expect the president to appoint people they like. Social conservatives do. And for them, appointments to the Supreme Court matter most of all.

As they see it, liberal activist judges have seized, without constitutional justification, the power to ban prayer from schools, to allow the unborn to be murdered and (in Massachusetts and doubtless soon elsewhere) to allow homosexuals to marry. This could be Mr Bush's last chance to push the court rightwards before President Hillary Clinton whacks it back left again. There are dozens of appellate-court judges with solid conservative credentials whom he could have picked to replace Sandra Day O'Connor, the centrist who is retiring. Instead of which, Mr Bush chose an unknown and told his foot-soldiers: “Trust me.”

Many religious conservatives are inclined to give Mr Bush the benefit of the doubt. Ms Miers is a born-again Christian who once gave $150 to an anti-abortion group and who once said, in response to a questionnaire from a gay-rights group, that she opposed overturning a Texan ban on sodomy. But it is unclear how much can be read into these biographical nuggets.

Ms Miers may believe that abortion is a sin, but it does not follow that she would therefore vote to overrule *Roe v Wade*, the 1973 Supreme Court decision that made abortion a constitutional right. How she votes on the court ought properly to be determined not by her personal beliefs, but by her understanding of the law. Does she think that *Roe v Wade* was such a blatant misreading of the constitution that it should be overturned? Or does she think it has been around so long that, whatever the faults of the original ruling, its precedent should be respected?

As for the issue of gay rights, in that same questionnaire, Ms Miers said she supported equal civil

rights for gays, which could include the right to adopt children. Liberals briefly panicked on October 3rd when Mr Bush praised Ms Miers's volunteer work for the Exodus Ministries, which many confused with Exodus International, an evangelical group that seeks to turn gays straight. In fact, it is a charity for rehabilitating ex-convicts.

And so it goes on. Ms Miers is now so close to Bush that she is nick-named his “work wife”. Yet, in the late 1980s, she donated money to the campaigns of Democrats such as Al Gore. Mr Bush says he knows her “heart”, but he once said the same of Russia's president, Vladimir Putin. Ms Miers is the most obscure nominee for decades and the harbinger, it seems, of a worrying trend.

Mr Bush clearly believes, correctly, that it is easier to get his nominees confirmed by the Senate if their views are unknown. His previous nominee, Mr Roberts, was quite hard to pin down but so obviously qualified that roughly half the Democrats in the Senate voted for him (along with all the Republicans).

Caligula's horse had a track record

Ms Miers is less qualified and more opaque, but still likely to be confirmed. This is not just because the Republicans have 55 of the 100 Senate seats, and, despite their doubts, none of them seems likely to oppose Mr Bush. It is also because the Democrats, not knowing much about her, have no compelling reason to filibuster her. (This process of preventing a vote from taking place is the only way a minority can block an appointment. It is an extreme tactic, and moderate Democrats have promised that they will use it only in exceptional circumstances.)

In the future, presidents of both parties are likely to prefer “stealth” nominees like Ms Miers. This will have two harmful consequences. First, appointments will become more like the lottery Ms Miers once ran. No matter how good a judge of character a president may be, he will find it tougher to pick dazzling jurists if he excludes from his search judges with a long record of judging hard cases and academic lawyers with a long history of debating controversies with their peers.

Second, if obscurity is to be rewarded, the most ambitious lawyers will shy away from writing articles for law reviews or expressing clear opinions in public. That will surely stultify debate about the proper role of the law in America—hardly a trivial matter in the most legalistic society on earth.

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Tom DeLay

Three strikes and you're out?

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The charges just got worse, but the prosecution may be rattled

AP

No delay

AN EPIC legal battle is shaping up in Texas. Last week, Tom DeLay was forced to resign his post as House majority leader after a Texas grand jury indicted him for conspiring to violate the state's election code. This week, more charges appeared. A different grand jury, on its first day of work, “re-indicted” Mr DeLay and two associates on charges of money-laundering and criminal conspiracy. The maximum penalty for money-laundering, a first-degree felony, is life in prison.

Re-indictments are not uncommon in Texas, where defence lawyers try to dismiss the originals with all kinds of technicalities (for example, if the indictment does not end with the words “against the peace and dignity of the state”, it gets tossed). Indeed, James Ellis and John Colyandro, the two DeLay associates also named in the conspiracy and money-laundering charges, have now been re-indicted more than once.

Still, the new charges, coming so quickly, are a surprise. Like those last week, they stem from the 2002 Texas election, when Mr DeLay masterminded the Republican campaign for the legislature. Ronnie Earle, the Austin-based prosecutor, claims that Mr DeLay's then political action committee, Texans for a Republican Majority (TRMPAC), collected corporate money and sent a cheque for $190,000 to part of the Republican National Committee. The RNC, at the conspirators' suggestion, then sent $190,000 donated from individuals back to seven Republican candidates' campaigns. This got round the Texan election code's ban on companies donating to state campaigns.

Mr DeLay has accused Mr Earle, a Democrat, of “prosecutorial abuse.” His defence lawyer, Dick DeGuerin, filed a motion on Monday to dismiss last week's indictment. Mr DeGuerin argued that the “conspiracy” charge started applying to the election code only in 2003, after a change made by the state legislature. Hours later came the re-indictment, leading Mr DeLay's defence team to boast that Mr Earle had realised that the original indictment was flawed.

Mr Earle claims that “additional information” arose in the days after the first indictment. Rubbish, reply Mr DeLay's lawyers, who also gleefully point to Mr Earle's admission that a third grand jury refused to issue a money-laundering indictment late last week. Meanwhile, the Austin legal world is buzzing with speculation about links between the defence's motion to dismiss the conspiracy charge and Mr Earle's re-indictments.

Mr Earle is probably worried about two things: Mr DeGuerin and timing. Mr DeGuerin, who started working for Mr DeLay only last month, is one of the best defence lawyers in Texas. “If you're a

wealthy person in Houston and you're guilty, you always hire Dick DeGuerin," says one Austin lawyer (a comment that is obviously not applicable to Mr DeLay who has long maintained his innocence).

Mr DeGuerin says he will seek to re-instate the three-year statute of limitations for Mr DeLay, who previously had signed a waiver. That would explain why the prosecution has had to hurry up: the allegedly illegal payments totalling $190,000 by the Republican National Committee took place on October 4th 2002. In any case, the fireworks begin soon: Mr DeLay's first day in court comes on October 21st.

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Economist.com WORLD NORTH AMERICA

Evolution and intelligent design

Life is a cup of tea

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How should evolution be taught in schools? This being America, judges will decide

HALF of all Americans either don't know or don't believe that living creatures evolved. And now a Pennsylvania school board is trying to keep its pupils ignorant. It is the kind of story about America that makes secular Europeans chortle smugly before turning to the horoscope page. Yet it is more complex than it appears.

In Harrisburg a trial began last week that many are comparing to the Scopes “monkey” trial of 1925, when a Tennessee teacher was prosecuted for teaching Charles Darwin's theory of evolution. Now the gag is on the other mouth. In 1987 the Supreme Court ruled that teaching creationism in public-school science classes was an unconstitutional blurring of church and state. But those who think Darwinism unGodly have fought back.

Last year, the school board in Dover, a small rural school district near Harrisburg, mandated a brief disclaimer before pupils are taught about evolution. They are to be told that “The theory [of evolution] is not a fact. Gaps in the theory exist for which there is no evidence.” And that if they wish to investigate the alternative theory of “intelligent design”, they should consult a book called “Of Pandas and People” in the school library.

Eleven parents, backed by the American Civil Liberties Union and Americans United for Separation of Church and State, two lobby groups, are suing to have the disclaimer dropped. Intelligent design, they say, is merely a clever repackaging of creationism, and as such belongs in a sermon, not a science class.

The school board's defence is that intelligent design is science, not religion. It is a new theory, which holds that present-day organisms are too complex to have evolved by the accumulation of random mutations, and must have been shaped by some intelligent entity. Unlike old-style creationism, it does not explicitly mention God. It also accepts that the earth is billions of years old and uses more sophisticated arguments to poke holes in Darwinism.

Almost all biologists, however, think it is bunk. Kenneth Miller, the author of a popular biology textbook and the plaintiffs' first witness, said that, to his knowledge, every major American scientific organisation with a view on the subject supported the theory of evolution and dismissed the notion of intelligent design. As for “Of Pandas and People”, he pronounced that the book was “inaccurate and downright false in every section”.

The plaintiffs have carefully called expert witnesses who believe not only in the separation of church and state but also in God. Mr Miller is a practising Roman Catholic. So is John Haught, a theology professor who testified on September 30th that life is like a cup of tea.

To illustrate the difference between scientific and religious “levels of understanding”, Mr Haught asked a simple question. What causes a kettle to boil? One could answer, he said, that it is the rapid vibration of water molecules. Or that it is because one has asked one's spouse to switch on

the stove. Or that it is “because I want a cup of tea.” None of these explanations conflicts with the others. In the same way, belief in evolution is compatible with religious faith: an omnipotent God could have created a universe in which life subsequently evolved.

It makes no sense, argued the professor, to confuse the study of molecular movements by bringing in the “I want tea” explanation. That, he argued, is what the proponents of intelligent design are trying to do when they seek to air their theory—which he called “appalling theology”—in science classes.

Darwinism has enemies mostly because it is not compatible with a literal interpretation of the book of Genesis. Intelligent designers deny that this is why they attack it, but this week the court was told by one critic that the authors of “Of Pandas and People” had culled explicitly creationist language from early drafts after the Supreme Court barred creationism from science classes.

In the Dover case, intelligent design appears to have found unusually clueless champions. If the plaintiffs' testimony is accurate, members of the school board made no effort until recently to hide their religious agenda. For years, they expressed pious horror at the idea of apes evolving into men and tried to make science teachers teach old-fashioned creationism. (The board members in question deny, or claim not to remember, having made remarks along these lines at public meetings.)

Intelligent design's more sophisticated proponents, such as the Discovery Institute in Seattle, are too polite to say they hate to see their ideas championed by such clods. They should not be surprised, however. America's schools are far more democratic than those in most other countries. School districts are tiny—there are 501 in Pennsylvania alone—and school boards are directly elected. In a country where 65% of people think that creationism and evolution should be taught side by side, some boards inevitably agree, and seize upon intelligent design as the closest approximation they think they can get away with. But they may not be able to get away with it for long. If the case is appealed all the way to the Supreme Court, intelligent design could be labelled religious and barred from biology classes nationwide.

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New Jersey

So what's in it for you, Jon?

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Everybody suddenly wants to clean up New Jersey

AP

WHEN something costs you $63m, you probably want it to last a lifetime. Not so Jon Corzine, a former chairman of Goldman Sachs, who spent that sum campaigning to win a Senate seat for New Jersey in 2000. And already Mr Corzine has had enough. He wants to be governor of New Jersey instead.

Mr Corzine may well have his way, though the fight is getting tougher as November's election approaches. His Republican challenger, Doug Forrester, has closed the gap after doing well in a television debate. Polls last week put Mr Forrester four to ten percentage points behind the Democrat; a month ago the gap was ten to 20 points.

Mr Corzine, who still has about $260m to his name despite an expensive divorce, can afford to buy plenty more air-time if needed. But Mr Forrester, who has made a smaller fortune from a health-care business, is also spending heavily, and the campaign is getting tetchier. The Forrester camp calls Mr Corzine a tax-raiser. The Corzine camp calls Mr Forrester an “extreme” Republican and a creature of George Bush.

But a suffocating legacy of local political scandal supplies the most constant campaign theme. New Jersey has long been notorious for handing out public-sector contracts to political donors, a corrupting practice known locally as “pay-to-play”. Mr Corzine and Mr Forrester both pledge to fight cronyism—though Mr Forrester has scored campaign points by sniping that some of the state Democratic Party's most notorious wheeler-dealers have necessarily been among Mr Corzine's allies since his move into politics.

The previous governor, James McGreevey, a Democrat, resigned a year ago after declaring himself a “gay American” embroiled in an adulterous relationship with an adviser who accused him of sexual harassment. Mr McGreevey's stand-in, Richard Codey, president of the state Senate, has done a good job helping the Democrats to regain their poise, and might have been a strong candidate for governor, save for Mr Corzine's intervention.

A shadow flitted across Mr Corzine's anti-cronyist credentials in August when he was shown to have lent and later given $470,000 to an ex-girlfriend who also happened to be local boss of a big public-sector labour union. Mr Corzine said it was a private matter, and claimed that he would be able to negotiate with her impartially as governor.

The top New Jersey job is a more than usually powerful one. The governor is the only statewide elected official. If Mr Corzine wins in November, one of his main tasks (other than cleaning up

state politics) will be to do something about New Jersey's locally levied property taxes, the highest in America, and another big campaign issue. Mr Forrester is promising, in effect, to reduce property taxes for most households by 30% over three years. Mr Corzine, more modestly, wants to boost an existing programme of rebates for needier households, and points out that Mr Forrester actually raised local property taxes when he was a town mayor in the 1980s.

Mr Corzine claims he can find money for more property-tax rebates and better public services by cutting wasteful spending, a common politician's claim which may, nonetheless, be truer in New Jersey than in many other places. He says Democrats are good for growth, pointing to Bill Clinton's presidency. New Jersey can only hope he is right. It did well shifting from a metal-bashing industrial economy in the 1970s to a high-tech and service economy by the 1990s, just across the river from Manhattan. But the current decade has seen much slower growth, especially in private-sector jobs.

Even voters who have warmed to Mr Corzine may wonder at his motives. Why, as one local newspaper put it, would he leave the thin air of Capitol Hill “to get muddy in New Jersey's political pigsty?” The answer seems to be that Mr Corzine, a courteous and bearded man who looks more like a professor than an ex-investment banker, has found a Republican-dominated Senate a frustrating place for a self-described “progressive” Democrat with a voting record well to the left.

If John Kerry had won last year's presidential election, and if the Democrats now held the Senate, Mr Corzine might be treasury secretary today, or a Senate kingpin. But as a relatively junior member of a minority party in Congress, he may have years ahead of him asking questions in committees, burnishing his voting record, climbing up the pecking order, and hoping for a political swing that will put his party in the majority. Alternatively, he could try to storm the New Jersey statehouse, and be master there from day one. Put like that, his choice is easier to understand.

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Economist.com WORLD NORTH AMERICA

Colorado's fiscal dilemma

To cut or not to cut

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A tough decision for voters and Republicans in particular

IS COLORADO'S Republican governor a business-friendly pragmatist or a spendthrift traitor? A few years ago, Bill Owens was often mentioned in conservative circles as a possible successor to George Bush. His star has fallen since. Now Mr Owens stands accused of trying to destroy one of the right's proudest achievements: Colorado's influential “taxpayer's bill of rights” (TABOR), which has returned some $3.2 billion to taxpayers over the past 13 years.

TABOR, which was passed by voters in 1992, pegs government spending to the growth in population and consumer prices, and gives any surplus revenue back to the voters. On November 1st, Mr Owens is asking the state's voters to suspend it for the next five years. The governor, who will be term-limited out of office in January 2007, says the mechanism needs to be adjusted to keep on working. Marc Holtzman, a Republican “friend” bidding to be his successor, says that would amount to “the largest tax grab in Colorado history”.

The adjustment comes in two forms: Referendum C would keep the $3.1 billion surplus expected over the next five years and divide 90% of it equally between schools, health-care programmes and community and state colleges. The remaining 10% would go to repay bonds worth $1.56 billion raised by Referendum D; these will be used mainly to improve Colorado's roads, bridges and schools. In addition, beginning in 2011, the state's income tax would be cut from 4.63% of federal taxable income to a mere 4.5%.

Mr Owens's gamble matters not just for Colorado, but for 27 other states that have enacted some form of tax and expenditure limitation (TEL). The beauty of TABOR is that it is part of the state constitution and so protected from legislative whim. Barry Poulson, a University of Colorado professor who delights in grading the nation's TELs, says Colorado's is “the most effective TEL in the country” and marks it “A-minus”; by contrast, some 20 states get an “F”.

So what has gone wrong? The answer comes in two parts. First, the very same voters who like their TABOR-imposed tax refunds perversely approved a constitutional amendment in 2000 that requires spending on public schools to rise annually at inflation plus 1% for ten years, and by inflation in all future years.

Second, hit by the end of the dotcom boom and tourism-destroying wildfires, Colorado slumped into recession in 2001. Over the three fiscal years from July 2001 to June 2004, Mr Owens had to cut spending per head in real terms from the state's general fund by 5.8%, 7.4% and 2.2%. Since the schools were protected, the cuts had to be made elsewhere: in higher education, health care, transport and so on.

Hence the present problem. The TABOR limits have been irrelevant for the past three years, because the dismal economy meant there was no increase in government revenue and spending. But with the economy now recovering, the TABOR limits kick in again—with the recession level of spending as their baseline. In the meantime the population has increased.

This “downward ratchet” has made many independents reconsider TABOR. The Bell Policy Centre, a non-partisan Denver think-tank, points out that Colorado is already 48th in the nation in state spending on higher education per $1,000 of personal income; 50th in providing children with on-time immunisation; 31st in hospital spending; and 35th for funding roads and highways. Bell's president, Wade Buchanan, points out that TABOR's inflation measure, the consumer price index, rises slower than government spending. A better TABOR, he argues, would have had a rainy-day fund and would have limited spending to 6% of the economy.

Mr Owens has thus won quite a lot of support from businesspeople for his referendums. But true believers see no need to change: there are inefficiencies still to be squeezed out of the system. Why not, asks Alison Acosta Fraser of the Heritage Foundation, “consolidate administrative functions, such as accounting and human resources, across all state agencies?”

The difficulty is that you can squeeze only so much before services are cut beyond what most people—even in libertarian-inclined Colorado—consider sensible. A no vote in November would force Mr Owens into the kind of budget surgery that makes governors deeply unpopular. For the moment he affects not to worry: “I'm not running for president,” he says. “The backlash won't be against me, but against my party.”

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Economist.com WORLD NORTH AMERICA

Agriculture

Follow the map

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Another cow disease with a possible link to humans

CRITICS of America's cattle industry like to claim that its main problem with bovine spongiform encephalopathy (BSE—or mad-cow disease) is refusing to admit that it has a problem. That charge is perhaps even more pertinent when it comes to a lesser known ailment, *Mycobacterium avium* subspecies *paratuberculosis*, more commonly known as MAP.

This hardy bacterium has been found in soil and water, and it boasts qualities a cockroach dreams about. It survives extreme temperatures and can lie dormant for months before orally infecting its host. Most often, cows become infected with MAP at birth. If they do, it can develop into Johne's (pronounced Yo-nees), an incurable wasting disease which can reduce beasts to pitiable, diarrhoea-racked skeletal creatures in their last days.

MAP is extremely common: the last big survey, back in 1996, found that one in five dairy herds had the disease, with that proportion doubling among big herds with more than 300 cows. The numbers have probably risen since then. Johne's costs the dairy industry alone $250m a year in lowered production and early cow culling, according to the Agriculture Department.

Left at that, the sickness would probably be just another ghastly farming disease (cattle get anthrax as well). But researchers are investigating whether Johne's is linked to Crohn's disease in humans. The diseases share similar symptoms; Crohn's is an inflammatory bowel disease characterised by chronic, sometimes crippling, diarrhoea. Several scientists suspect that some people may have a genetic susceptibility to developing Crohn's—possibly by drinking milk infected with MAP.

The government and the industry both insist that pasteurisation—heating up milk to a high temperature for a short period—kills any MAP that gets into it. But a recent study of pasteurised whole milk in shops by researchers at Marshfield Clinic Laboratories in Wisconsin found traces of the bug in 2.8% of the samples. This has left the industry in an awkward position: it needs more government money to fight the disease, but kicking up a fuss about it sours milk's wholesome image.

The government officially launched a Johne's control programme three years ago. But the White House is preoccupied by bioterrorism and mad-cow disease: and it wants to trim the budget deficit. The current budget cut next year's allocation for Johne's disease from $19m to $3m.

This reflects the fact that few politicians have heard of Johne's, and the industry seems unsure how much to tell them about a disease which carries a stigma even in the cattle industry. “It's like you have the plague,” admits Jackie Menn, a Wisconsin farmer, whose herd of 85 Jersey cows is infected. Her herd is taking part in a joint federal-state programme to control the disease (which includes culling sick cows). Wisconsin has signed up for the national programme, which is voluntary; but several other cattle states, including Wyoming and Montana, have not.

The biggest problem may lie in California. The average dairy herd there had 806 cows in 2003; some farms boast thousands of animals and they are often kept in close proximity. The state has 55 dairy herds in its control programme, but that leaves another 2,070 to go—and that does not include beef farms.

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Lexington

Hold the champagne

Oct 6th 2005
From The Economist print edition

The Democrats cannot rely on the Republicans' current woes to deliver victories in 2006 and 2008

TALK about trouble coming not in single spies but in battalions. For much of his first term, almost everything that George Bush touched turned to political gold. He even managed to parlay a badly-handled war in Iraq into a vote winner. But now almost everything he touches turns to dust.

The Democrats are quietly jubilant. They are seizing every chance they can get—and there are plenty of them—to brand the Republicans as the party of "corruption and cronyism". They seem to be recruiting good candidates for next year's elections. Some even wonder whether 2006 may be their equivalent of 1994—when the Republicans won 52 seats in the House and nine in the Senate, ending 40 years of Democratic rule.

They should hold the champagne. Parties don't win elections just because their rivals hit a rough patch. They win them because they win the battle of ideas, because they think ahead and cook up cogent policies, because they offer a positive vision of the future. Bill Clinton did this brilliantly in 1992. Tony Blair did it even more brilliantly in 1997. But, so far, not the Democrats.

Can anyone name a single exciting Democratic idea for dealing with poverty? Or crime? Or reforming the public sector? Or winning the *Kulturkampf* with Islamic extremism? In fact, can anyone name a single exciting Democratic idea, full stop? The Democrats have squandered their years in opposition railing against the Republicans rather than recharging their intellectual batteries. They may be winning a few political battles of late—largely because of Republican incompetence. But they are losing the vision wars.

The reason for this is as simple as it is potentially lethal: the Democrats are split down the middle

on everything from Iraq to gay marriage. Centrists believe in working with business, protecting family values and fighting terrorism. “We believe that the September 11th attacks changed America for ever,” says the Democratic Leadership Council (DLC), “and defeating terrorism is the supreme military and moral mission of our time.” Liberal activists believe the opposite: that corporations are bad, family values are hogwash, and the war on terror a delusion.

Worse still, the wrong side is getting the upper hand. A new generation of angry young activists have used their mastery of the internet to tilt the party to the left. Groups such as Moveon.org (which claims 3.3m members) and blogs such as the Daily Kos (which has thousands of partisans venting daily) now colour the whole tone of the political debate on the left.

The teenage scribblers of the left seem to be turning the Democrats into a deranged version of Pavlov's dog—reacting to every stimulus from Professor Rove's laboratory rather than thinking ahead. Look what has happened in Congress, where the combination of a re-energised left and a ruthlessly partisan White House is making life miserable for would-be centrists. In 1994, 102 House Democrats voted in favour of NAFTA; this year, only 15 voted in favour of CAFTA, a more modest free-trade deal.

The teenage scribblers are wedded to a suicidal strategy: they think that their party's best chance of winning lies not in emulating Mr Clinton and moving to the centre but in emulating their nemesis, Mr Bush, and motivating their base. This ignores the most salient fact about American politics: there are three conservatives for every two liberals. The Democrats cannot win without carrying about 60% of moderates.

The other dysfunctional party

Is it really that bad? Marshall Wittmann, of the centrist DLC, counsels against despair about the party's future. He points out that the anti-Bush left has a built-in sell-by date: Mr Bush will not be running in 2008. He also argues that the person who defines the character of a party is its presidential candidate—and the strongest candidates for 2008, such as Hillary Clinton and Mark Warner, are forward-thinking moderates.

There are two problems with Mr Wittmann's optimism. The first is that Moveon et al will still be in full bark against Mr Bush in 2006. That will not help in a contest where the tables are already stacked against the Democrats. In the Senate, they will be defending seven potentially vulnerable seats while the Republicans will be defending five; in the House, 41 Democrats are defending districts that Mr Bush carried in 2004 while only 18 Republicans are protecting districts that John Kerry carried.

Second, even if a centrist Democrat succeeds in winning the party nomination in 2008, he or she will have a huge mountain to climb. In “The Politics of Polarisation”, a new paper published by the Third Way group, William Galston and Elaine Kamarck, two centrist stalwarts, lay out the topography. The public is profoundly sceptical of the Democrats on both “values” (only 29% of Americans regard the party as friendly towards religion) and defence (it is no accident that the Democrats have won the popular vote only in recent elections—1992, 1996 and 2000—when national security was all but absent from the debate). The party has also lost ground with two groups of swing voters: married women favoured them by four points in 1996, but backed Mr Bush by 12 points in 2004; a 16-point lead among Catholics became a five-point loss in 2004.

The 1990s showed that left-of-centre parties can climb the highest mountains provided they start early and stick to the right path. Mr Clinton made his political reputation as a reforming governor who was willing to think afresh about everything from education to free trade. No sooner was Mr Blair elected leader of the Labour Party in 1994 than he started tearing up left-wing shibboleths

about public ownership and rebranding the party as “New Labour”. So far the Democratic Party has been so paralysed by its internal contradictions that it has wasted its years in opposition. Perhaps it will start laying out a blueprint for government soon. But time is short.

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Mexico

Righting the scales

Oct 6th 2005 | MEXICO CITY AND OAXACA
From The Economist print edition

The long path towards justice

Get article background

THE justice system in Mexico is on its knees. The innocent are imprisoned and criminals go free. The poor go to jail. The rich don't. Drug-trafficking, and the violence it brings, may attract most international attention, but the flaws in the organisation of Mexico's courts and police affect far more people than the “narcos” ever do.

The first step in fixing a problem is to admit you have one. “Our legal justice system has collapsed,” says Patricia Villanueva, chief prosecutor in the southern state of Oaxaca. “It is obsolete,” agrees Manuel Moreno Rivas, head of the state's judicial police, responsible for investigating crimes. That is why Oaxaca, along with half a dozen or so of Mexico's 32 states, is seeking to revolutionise its judicial system. Drawing on successful programmes in Chile and Costa Rica, it aims to move from a Napoleonic inquisitorial system, where prosecutors take most of the decisions and judges act largely as rubber stamps, toward a more British- or American-style adversarial system, in which oral arguments before a judge in court play a key role.

According to Guillermo Zepeda, a researcher at CIDAC, a think-tank in Mexico City, 95% of crimes in Mexico fall under local jurisdiction. As a result, reforms at the state level are likely to have a more profound impact on the nature of crime and punishment in Mexico than action at the federal level. In any case, attempts to address structural problems at the federal level have stalled politically. The hope is that the patchwork effort to overhaul state systems will eventually “trickle

up” to the federal level too.

Of every 100 crimes in Mexico, it is estimated that only 20 or so are reported. In Oaxaca, only four or five of those 20 are actually investigated, Mr Moreno says, a figure broadly representative of the country as a whole. Furthermore, of the investigations that are opened, more than three-quarters are never resolved. There is also a strong selection bias. Because prosecutors have a weekly quota of indictments to meet, says Layda Negrete, a professor at CIDE university in Mexico City, the crimes which are prosecuted are either overwhelmingly minor ones or crimes where the perpetrator was caught red-handed. According to a 2003 survey by CIDE, over 60% of the prison population was caught *inflagrante* and more than half was there for minor, non-violent crimes. As a result, says Ana Magaloni, also of CIDE, Mexican jails are “stuffed full of poor people”, while professional criminals are not caught.

The underlying aim of the judicial reforms, which are broadly similar across the states seeking to implement them, is to increase transparency and efficiency, thereby supposedly prompting prosecutors and police to do a better job. Though there is some corruption, the main problem, according to Ms Magaloni, is incompetence. Everyone agrees on the need to set up training schemes for police, lawyers and judges, but this will not be easy. As José Antonio Caballero of Mexico City's National Autonomous University notes, at present there is no national bar association nor even a programme of accreditation for law schools.

Torture

If the state of Mexico's lawyers is bad, that of its police is arguably much worse. “It's a myth that the top level knows what's going on,” Ernesto López Portillo of the Institute for Security and Democracy in Mexico City says: “Real control rests with mid-level commanders.” So when Mr Moreno and Ms Villanueva deny that prisoners are beaten or tortured, they may be in earnest, despite evidence to the contrary.

Following his arrest in Oaxaca last year, Habacuc Cruz Cruz, a union organiser in the state, says that he was severely beaten and kept for three to eight days at a time in a tiny cell without light or ventilation, which measured just one square metre. Mr Moreno insists that such treatment no longer takes place; the penal system could not withstand the public outcry if it did, he says. But, as Ms Magaloni dryly comments, Mexicans have lost their capacity to react to scandal. Cases like Mr Cruz Cruz's no longer shock. Without a thorough overhaul of the police system as well, judicial reform will be futile, Mr Lopez Portillo argues.

So far, only the northern state of Nuevo León has actually started implementing reforms. Cases involving minor crimes are now argued orally in front of a judge, instead of the judge reading mounds of papers alone in chambers. This, Mr Zepeda says, has already produced big gains in efficiency and equity. In Oaxaca, the state government hopes to pass legislation in the coming legislative term (ie, the next six months) to launch a five-year reform process leading to the formal installation of a new legal system.

But even if all goes well at state level, the lack of change at the federal level could cause difficulties. Under a process called *amparo*—a challenge to the constitutionality of a local decision—almost any legal matter can be appealed to the federal courts. While only 2% of state cases at present go to *amparo*, Roberto Hernández of CIDE says that this is sufficient to clog the federal system. Some two-thirds of appealed cases are dismissed by the federal courts, often on minor technical grounds. Unless the procedure is changed to one where appeals are possible only on specific legal grounds, there is a risk that, as today, anyone with the means could file for an almost limitless number of *amparos*, says Mr Hernandez, effectively neutering the state system.

Juan de Jesús Vásquez, a state appeals court judge in Oaxaca, believes the judicial reform plans represent a 180 degree change of course. But, he cautions, “many of us haven't been to law school in 25 years”, so this would be difficult to achieve. The fruits of the reforms, he concedes, “are for my kids and grandkids”. It will be a long time before Mexico has a justice system worthy of the name.

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Economist.com WORLD LATIN AMERICA

Argentina

Another wig falls

Oct 6th 2005 | BUENOS AIRES
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The removal of a fifth Supreme Court judge threatens the separation of powers

Get article background

SHORTLY after assuming Argentina's presidency, Carlos Menem pushed through one of the brashest court-packing moves in recent memory. In a brief session in April 1990, his Congress added four more seats to the five-member Supreme Court. This, plus the replacement of one of the pre-existing justices, enabled Mr Menem to create a notorious “automatic majority” of mostly legally undistinguished loyalists, who religiously backed his executive initiatives of dubious constitutionality.

Since Néstor Kirchner became president two years ago, he has dedicated himself to ridding the government of Mr Menem's taint, particularly in the judiciary. Three justices from the bloc have resigned, while a fourth was forcibly discharged in December 2003. The Senate finally removed its last, Antonio Boggiano, from the court on September 28th after finding him guilty of arbitrary, biased and inconsistent rulings. Yet while Mr Kirchner has hailed previous reversals of Mr Menem's decisions, he has kept mum on the latest removal, fuelling speculation that he might have rather had Mr Boggiano stay.

Unlike the other members of the “automatic majority”, Mr Boggiano was a respected jurist before joining the court and, while indubitably a tool of Mr Menem in the 1990s, has more recently demonstrated his independence. To Mr Kirchner's delight, he voted with the majority in June to overturn Mr Menem's pardons of military officers for human-rights violations. He further endeared himself to the government by ruling conclusively in favour of the constitutionality of “asymmetric pesification”—the decision by Mr Kirchner's predecessor, Eduardo Duhalde, to convert Argentine banks' dollar-denominated deposits into pesos at a 1.40 exchange rate, while swapping over their loans at the old one-to-one figure, during the January 2002 financial crisis. This won him the backing of Mr Kirchner's chief of staff, Alberto Fernández, as well as the support of the economy and foreign ministers.

Along with the recent voluntary retirement of another justice, Mr Boggiano's departure has created two more vacancies on the court in addition to the four that Mr Kirchner has already filled. Although the president has won widespread praise for making the nomination process more transparent and selecting eminent and independent judges, the possibility of his naming two-thirds of the country's highest court hardly bodes well for the separation of powers.

Congress's Justice Committee, chaired by a loyalist of Mr Duhalde (Mr Kirchner's former political patron and current rival), has proposed that the president reduce the court to seven members rather than select two more nominees. To reject the plan, which has broad support from Argentina's leading think tanks and advocacy groups, would endanger Mr Kirchner's legacy as a benevolent judicial reformer. But to go along with it would deny him an opportunity to plant reliable votes on the court. Although Mr Kirchner has not yet rejected the proposition, Mr Fernández, his preferred mouthpiece, has left little doubt as to the president's views, calling the

plan a “wicked move intended to destabilise the government”.

Meanwhile, Mr Boggiano has not given up hope of regaining his seat on the court. He plans to appeal to the Inter-American Court of Human Rights. Despite Mr Kirchner's distaste for meddling by such international bodies—and his desire to cleanse Argentina of any Menemist footprints—a lifeline for the ex-justice, however unlikely, might do the president a favour.

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Economist.com WORLD LATIN AMERICA

Abortion in Latin America

Last bastions

Oct 6th 2005 | BOGOTá
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A challenge to Colombia's abortion laws could lead to wider liberalisation

ONLY a handful of countries continue to ban abortion totally, even when the mother's life is in danger. Colombia is one of them. Earlier this year, its Congress increased the maximum sentence for violators to four and a half years in prison. Yet every year, an estimated 400,000 desperate women prefer to run the risk of jail and dangerous backstreet abortions rather than give birth to an unwanted, possibly severely handicapped baby, or a child resulting from rape or incest.

Illegal abortions are the third cause of maternal mortality in this predominantly Catholic country. Colombian women's groups have long been campaigning for decriminalisation. United Nations bodies responsible for monitoring international human-rights conventions have lent the movement their weight, arguing that Colombia's draconian laws violate a woman's fundamental right to life and health. Public opinion is in favour of greater liberalisation when the mother's life or health are at risk, or when the fetus is severely deformed. Yet repeated attempts in Congress to amend Colombia's penal code have hitherto failed.

Not much choice
Abortion in Central and Latin America
Prohibited under all circumstances
Chile, Colombia, El Salvador, Honduras, Suriname
Prohibited except when life of mother endangered
Brazil*, Guatemala, Mexico*, Nicaragua, Panama*†, Paraguay, Venezuela
Prohibited except when life and physical health of mother endangered
Argentina‡, Bolivia*§, Costa Rica, Ecuador‡, Peru, Uruguay*
Permitted for socio-economic reasons, as well as when life or health of mother at risk
Belize†
Abortion on demand
Cuba, French Guiana**, Guyana††
*Permitted in case of rape
†Permitted in case of fetal malformation
‡Permitted in case of rape when mother is considered mentally incompetent
§Permitted in case of incest
**Permitted only up to 14 weeks of gestation
††Permitted only up to 8 weeks of gestation
Source: Centre for Reproductive Rights

Now Monica Roa, a young Colombian lawyer working for Women's Link Worldwide, a women's rights group, is seeking to mount a legal challenge for the first time. In a suit filed in the Constitutional Court, she argues that a total ban on abortion is unconstitutional and violates Colombia's international treaty obligations. In an effort not to offend Catholics too much, she is calling for abortion to be permitted in just three instances: if the mother's life or health are at risk, if the fetus is severely malformed, or in the case of rape.

Ms Roa claims that the chances of passing a new abortion law are now higher than at any time in Colombia's history. She would appear to have good grounds for optimism. The Constitutional Court has already ruled in other cases that international law supersedes domestic law. International groups, including Yale and Harvard Law Schools, have filed briefs in support of her claim. And both Colombia's procurator-general's office and the Ministry of Social Protection have admitted that illegal abortions present a serious public health problem.

But Ms Roa's quest has brought her up against powerful enemies. In June, her office was broken into and two computers stolen, along with confidential files. She has now been assigned two bodyguards. Human Rights Watch, a New York-based lobby group, has expressed concern about

the safety of all those working on the case. Meanwhile, President Álvaro Uribe has rushed to assure the Catholic church that his signing of a treaty banning discrimination against women did not signify any support for abortion rights.

Ms Roa's chief opponent is José Galat, elderly Catholic rector of the University of Greater Colombia. He maintains that abortion is akin to the massacres carried out by Colombia's right-wing paramilitary groups. How can people complain about that violence if they allow mothers to assassinate the children in their wombs, he asks. He and his supporters have taken out gory advertisements featuring bloodied fetuses and have collected 2m signatures opposing any relaxation of the law.

Most countries of Central and Latin America—along with most of sub-Saharan Africa and southern Asia—have extremely restrictive abortion laws, usually allowing the termination of a pregnancy only to save a woman's life or protect her physical health. But Ms Roa believes there is now a momentum in the region toward greater liberalisation. A decision on the legality of Colombia's laws is due by mid-December. It could help determine whether that momentum becomes unstoppable.

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Uruguay

Paper dreams

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A battle over foreign investment

Reuters

We want to have our cake and eat it

ACROSS the River Plate from Argentina, Uruguay wasn't doing that badly until its big neighbour's economy collapsed four years ago, triggering a run on its banks. That provoked a sickening slump in Uruguay's own economy, with GDP falling by 11% in 2002. But unlike Argentina, Uruguay did not default on its public debt nor tear up its contracts. That is one reason why in April Metsa-Botnia, a Finnish company, began building a cellulose plant on the Uruguay River bordering Argentina. This month, Spain's ENCE plans to start a similar plant a few miles away. At a combined cost of $1.7 billion, the two installations amount to the biggest capital investment in Uruguay's history and are expected to give an important boost to its already impressive, though still fragile, recovery—that is, if environmental protesters and Argentina allow them to go ahead.

Argentina's government complains that Uruguay did not consult it about the plants, which, it says, will pollute the river, over which the two countries share sovereignty. A bi-national committee has been set up to look at this, but its report is not binding. To Uruguay's annoyance, Argentina is now trying to block a loan from the World Bank's International Finance Corporation to fund 9% of the plants' cost. The outcome of this battle matters much to Uruguay's president, Tabaré Vázquez, and his left-wing Broad Front government, elected last year. Mr Vázquez has maintained his predecessor's orthodox economic policy and, to the disappointment of green activists, has given his approval to the plants.

Pulp factories certainly do have a nasty environmental reputation. Opponents say that over 1m hectares (2.5m acres) of eucalyptus trees must be planted to supply the mills, threatening other local flora. Moreover, they complain that the Metsa-Botnia installation will not use the cleanest available production technology, meaning that it may emit potentially carcinogenic dioxins. But the plants' economic value is huge. Their total cost represents 11% of Uruguay's GDP and could add 1.5 percentage points a year to its growth rate. However, even more investments will be needed to sustain the country's recovery, which has so far brought unemployment down to 12%, from a peak of 20% three years ago.

Danilo Astori, the finance minister, wants to boost the share of investment in GDP to 20% by 2010. But despite Uruguay's stable institutions and governance, luring more projects like the cellulose factories to such a small market may be difficult. Public opinion is hostile to privatisation, committed to a large welfare state and wary of foreign investment. Uruguay's Congress has yet to ratify a proposed bilateral investment treaty with the United States.

Meanwhile, Mr Vázquez has been busy honouring some of his promises to his supporters. Despite an already inflexible labour market, he has given the unions even greater powers. He has ordered a reluctant Mr Astori, already struggling with a public debt equal to 85% of GDP, to budget for a rise in education spending as well as an emergency anti-poverty programme. While Uruguay's welfare state has served its democracy fairly well, someone has to pay for it. Uruguayans will hope that Argentina doesn't prevent the pulp firms from chipping in.

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Indonesia

Bali, again

Oct 6th 2005 | KUTA AND JAKARTA
From The Economist print edition

EPA

But Indonesia is resolutely unspooked

THE simultaneous explosions in three different restaurants on the evening of October 1st killed 19 people, as well as three suspected suicide bombers, and injured more than 100. But the Balinese, inured by the much deadlier attack of October 2002, which killed 202, seem determined not to be cowed this time around. Shopkeepers, restaurateurs and hoteliers insist that life will go on. Tourists, too, appear surprisingly stoical: on the morning after the blasts, more visitors were strolling along the waterfront than thronging the airport. Despite the continued bloodshed, the attacks suggest that Indonesia's three-year-old crackdown on Islamic terrorists is working, in that the terrorists have been reduced to softer targets, smaller bombs and cruder methods.

Indonesian officials suspect that Jemaah Islamiah (JI), the terrorist outfit behind the previous bombing in Bali, as well as two subsequent attacks in Jakarta, is also responsible for the latest outrage. After all, Azahari Husin, the group's suspected bomb-maker, remains at large. JI is the only organisation known to have used suicide bombers in South-East Asia in the past, most notably in the original Bali bombing. Moreover, a JI member arrested for his role in the bombing of the Australian embassy in Jakarta last year claimed that Mr Azahari was hoping to launch more frequent attacks.

But last weekend's bombings were different from previous ones in several important respects. First, they appear to have been conducted solely by pedestrians carrying or wearing bombs, without any vehicles being involved. Moreover, the bombs were made of TNT, rather than the more complex and bulkier chemical mixtures used by JI in the past. They also struck the softest of targets: a string of open-air restaurants spread along one of Bali's most popular beaches, and

another restaurant in the main shopping district of Kuta, Bali's biggest resort town. JI's last two attacks, by contrast, targeted the well-defended Marriott hotel in Jakarta and Australia's fortress-like embassy there.

Zachary Abuza, of Boston's Simmons College, argues that if the recent bombs are indeed the handiwork of JI, then the group is changing its tactics, presumably thanks to the increasingly successful international crackdown on it. Most of its top leaders are in jail, while cells have been uncovered in Malaysia, Singapore, Pakistan and Australia. Indonesia alone has arrested over 200 suspected members. Many of those who helped to funnel money from al-Qaeda to JI, such as the notorious Hambali, are also behind bars. Foreign embassies, luxury hotels and other obvious targets in Indonesia have greatly strengthened their security. This helped to reduce the casualties in the two Jakarta bombings, which killed 12 and 11 people respectively.

According to Mr Abuza, the use of smaller bombs made from TNT might be a sign that JI is having a hard time obtaining bomb-making material, or is running low on cash. The selection of targets without any security, and the decision to carry the bombs on foot rather than by car, might indicate that the group has less time or money for planning and training.

Sidney Jones, head of the Indonesian office of the International Crisis Group, a think-tank, points out that many of those implicated in the bombing of the Australian embassy last year were not actual members of JI, but friends or acquaintances of Mr Azahari and Noordin Muhammad Top, another fugitive leader of JI. Interrogations of captured JI members reveal a rift in the organisation: many are said to be unhappy about the number of Muslims killed by previous bombs and worried that the terrorist campaign is undermining support for Islamic activism. Miss Jones believes that Messrs Azahari and Noordin have effectively split from what remains of JI, and are now acting on their own initiative with other like-minded individuals.

All these developments, if borne out, constitute a qualified victory for the authorities: they are likely to make future bombings easier to mount and harder to foil, but less deadly too. The accounts of those convicted for the first Bali bombing suggest that it cost only $30,000 or so to mount. Last weekend's attacks must have cost much less. Nor is there any shortage of recruits, given Messrs Azahari and Noordin's many contacts in various extremist outfits. In March, an Indonesian arrested in the Philippines claimed to have worked at a training camp for JI and Abu Sayyaf, a Philippine militant group, from which 23 would-be terrorists had just graduated.

Most Indonesians, meanwhile, are learning to take terrorist attacks in their stride. The rupiah and the stockmarket, which were more attuned to the government's recent decision to cut fuel subsidies, actually gained ground after the latest bombing. The senior economics minister estimated that even if tourist numbers fell by half, the country's growth rate would slip by only half a percentage point.

Muslim politicians, however, are still having a hard time coming to terms with atrocities mounted in the name of their faith. Hidayat Nur Wahid, a former leader of the Islamically inclined Prosperous Justice Party and speaker of the country's top legislative body, suggested that promoters of rival tourist destinations, rather than Islamic militants, were behind the bombings. Other religious leaders have argued that Muslims could not be responsible, since Islam does not condone the murder of innocent bystanders. Liberal Muslims insist that a vigorous campaign is needed to discredit more militant interpretations of Islam, and thus to reduce the number of potential recruits to groups like JI. But persuading more conservative religious figures of that is as difficult, it seems, as catching Indonesia's remaining terrorists.

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Taiwan and America

Still waiting

Oct 6th 2005 | TAIPEI
From The Economist print edition

The island is wary of America's hardware

Get article background

WHEN George Bush took office in 2001, he made two bold commitments to Taiwan. The first was his declaration to do “whatever it takes” to help defend the Asian democracy, presumably against a China that claims the territory for its own. The second was to offer a package of advanced weapons, including submarines and anti-missile batteries, with which the Taiwanese could boost their defensive capacities. Four years on, there is no sign of these weapons arriving, since Taiwan has not approved a budget for them. The Bush administration is getting impatient.

Officials from the Department of Defence have let it be known that America is unenthusiastic about defending a Taiwan that apparently does not want to defend itself. Even the State Department has expressed frustration, with a senior official telling a congressional commission that America “wants results” on the weapons procurement.

There are many reasons for the delay. Taiwan's government, controlled by the Democratic Progressive Party (DPP), which supports the territory's formal independence from China, wants the arms; but the opposition Kuomintang (KMT) and People First Party, which between them control parliament, do not. Reasons for their opposition include their traditional support for reunification with China—they see the weapons as strengthening the hand of the separatists—and a new-found closeness to the government in Beijing: both parties' leaders visited China earlier in the year.

The DPP accuses them of being little more than paid agents for China's reunification policy. In reality the parties realise that, as Taiwan's economy becomes more bound up with China's, there is a need for negotiation across the Taiwan Strait that the DPP, cold-shouldered in Beijing, cannot meet.

But there is more to the stand-off than opposition obstruction. The government has shown timidity in trying to pay for the weapons, which cost around $16 billion, through a “special budget” rather than trying to win the argument for an expansion of the ordinary defence budget, which would mean making unpopular expenditure cuts elsewhere. And the opposition, particularly the business-oriented KMT, might just have been won over if America had offered Taiwan a role in the construction of the most expensive items on the list, eight submarines. This was, however, vetoed by the Defence Department in 2004.

The legislature's defence committee has now refused to review the budget some 31 times since June last year. Perhaps next year, says Wang Jin-pyng, the legislature's speaker and a senior KMT figure. America will have to wait.

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Economist.com WORLD ASIA

Japan and China

Oil and gas in troubled waters

Oct 6th 2005 | BEIJING AND TOKYO
From The Economist print edition

Two resource-hungry nations square off in the East China Sea

Get article background

FOR China and Japan this has been an exceptionally difficult year in an always troubled relationship. Among their many disagreements, which in April triggered the biggest anti-Japanese protests in communist China's history, is a long-simmering territorial dispute in the East China Sea that lately has taken a turn for the worse. With Japanese officials and politicians accusing China of deploying "gunboats", nationalist sentiment on both sides is complicating efforts for a resolution.

Two days of talks in Tokyo ended on October 1st with no agreement on the dispute, which focuses on the exploitation of undersea oil and gas deposits straddling what Japan says is the border line between the two countries' exclusive economic zones (EEZs). China does not recognise the border line and says that in any case its drilling is in an undisputed area. Japan says China's activities could suck gas from its side of the line.

Three weeks before the talks—the third round since October last year—the Chinese navy made a dramatic appearance near a Chinese drilling platform at the Chunxiao field (known by the Japanese as Shirakaba). It deployed five vessels, including missile-equipped destroyers and frigates. Last week, Japanese officials said that one of the boats had turned a gun turret—but had not locked its radar—on to a Japanese P3-C reconnaissance aircraft that was monitoring the activity. Keizo Takemi, a veteran politician who heads the ruling Liberal Democratic Party's parliamentary group on marine resources, calls this "gunboat diplomacy". As Mr Takemi puts it: "The Chinese side have used military power to leverage their political situation. The squadron was an attack squadron and its purpose was quite clear—to strengthen against the Japanese position. This is a really unfortunate development, for it could lead to the kind of vicious cycle that descends into military conflict."

Last week, China confirmed that it had set up a "reserve vessel squadron" in the East China Sea. Despite Japan's calls for drilling activities near the disputed border line to be suspended pending an agreement, Japan says it suspects that China recently began production of gas or oil at the Tianwaitian field (called Kashi in Japanese) near Chunxiao. The Japanese believe Tianwaitian's resources might also straddle the line.

Japan too has been stepping up the pressure. In July it granted drilling rights in the area, including in the Japanese-claimed side of Shirakaba, to a Japanese company, Teikoku Oil (it does not help that this means Imperial Oil). Were Teikoku to begin drilling, this would raise tensions

enormously, since the line China claims as the EEZ boundary puts the site well within China's side.

So who is in the right? Unfortunately, there is no clear answer. Under the UN's Convention on the Law of the Sea, an EEZ can extend up to 200 nautical miles from a country's shoreline. But the East China Sea between China and Japan is only about 360 nautical miles at its very widest. Japan says the boundary should be the median line between the two countries. China says its EEZ should extend to the edge of its continental shelf, which would put the line almost up against Japan's shores. The convention does not give specifics of how overlapping EEZ and continental shelf claims should be resolved.

There are some positive signs. Japan says it will be very careful not to be drawn into any tit-for-tat response to China's naval deployments. And China, though insistent at last week's talks on pushing its continental shelf approach, did not reject outright a proposal by Japan for joint development of fields straddling the median line. To Japan's annoyance, however, China did raise the issue of possible joint exploration near the Senkaku Islands—Diaoyutai in Chinese—which are controlled by Japan but claimed by China. Japan worries that China's efforts to focus on this area are intended to undermine Japan's sovereignty claim.

Mindful perhaps of the danger of rekindling the nationalist sentiment that erupted with such fury in Chinese cities in April, the official media in China have been low-key in their coverage of recent developments. A Japanese official says that his side has been trying to focus instead on the business potential of joint development. “Once it becomes a territorial issue, it can get very nasty and very difficult to solve,” he says. But it may already be too late.

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India

The fifth monarch

Oct 6th 2005 | DELHI
From The Economist print edition

Will Rahul sit on his great-grandfather's (and grandmother's and father's) throne?

Get article background

THERE is no democratic dynasty in the world to match that founded by Jawaharlal Nehru, India's first prime minister. For 39 of the 58 years since independence, one or other of his clan has been in charge—the latest of them being Sonia Gandhi, Italian-born widow of Rajiv Gandhi, who was Nehru's grandson and served as prime minister in the 1980s.

Sonia Gandhi leads the Congress party, which heads India's coalition government. Though she renounced the prime minister's job after last year's general election in favour of Manmohan Singh, a 73-year old technocrat, it is she who tugs the reins of government. Now there is growing speculation about Congress's prime ministerial candidate for the next general election, which is due by 2009 but could come earlier. The dynastic bet is on Mrs Gandhi's 35-year old son, Rahul, who became a member of parliament last year for Amethi, the family's political base in the northern state of Uttar Pradesh. By 2009, he will be nudging 40—which is the age of his father, Rajiv, when he became prime minister.

AFP

Rahul gets ready

But Rahul Gandhi, whose weekend hobby is racing motorbikes with friends on a private dirt track near Delhi, has refused to emerge as an iconic figure. Reports suggest that he is primarily concerned about marrying his long-term Spanish architect girlfriend—allegedly against the wishes of his mother, who is said to fear that further dilution of the dynasty's Indian bloodline would resurrect an anti-foreigner backlash that she herself endured.

Mr Gandhi has not made much of a mark as an MP, having spoken only once in parliament, and is prone to political gaffes. Last month he (accurately) told *Tehelka*, a weekly newspaper, that there was “no governance” in the state of Bihar—which was embarrassing since Bihar has been under direct rule by the Congress-led central government since April. He said he did what he liked, despite his mother's views, and appeared to boast (probably flippantly) that he could have been prime minister when he was 25.

So might the Gandhi family's sycophantic hangers-on switch to another icon, possibly Mr Gandhi's more politically astute and charismatic sister, Priyanka, who has withdrawn into family life over

the past year? Probably not. There is more to Mr Gandhi, who has worked for a British management consultancy and part-owns a Mumbai software company, than the caricature painted by India's gossip columns. The *Tehelka* interview (which Congress insists was an untaped background chat) revealed a straight-talking, sometimes naive, young man, with firm views and ambitions.

“My goal is to take India to number-one slot,” he is reported to have said, adding that his idea of politics was “very different from what is being done now”. He has made a few trips abroad, and regularly meets political, economic, development and business experts. Advisers keep him as quiet and out of the public eye as possible, fearing, as he puts it, that “every time I want to do something, it may go wrong”.

That will probably change soon. Mrs Gandhi is expected to make him a general secretary of the Congress party, which would force him into the public eye. Suhel Seth of Equus, a Delhi-based branding company, says he should align himself with a cause like education and shed the image of being “the chosen one”. That touches on the question of whether Mr Gandhi can grow by 2008 into someone who not only draws crowds and votes, but is acceptable to coalition partners. He says he is in for the long haul. So his mother could yet choose another interim prime minister, and save him for another day.

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Afghanistan

Not what the doctor ordered

Oct 6th 2005 | SHINWARI
From The Economist print edition

An alternative use for opium

AFP

Not from Afghanistan: legal dope

Get article background

AN ATMOSPHERE of despair prevails in the village of Shinwari, close to Nangahar province's border with Pakistan. This year's internationally-funded $860m blitz on Afghanistan's opium industry produced a 96% drop in the poppy hectarage in the province, the best result amid a 21% overall reduction nationwide. But farmers in Shinwari say that along with the poppy went 60-90% of Nangahar's rural economy, a void not being filled by promised “alternative livelihood” schemes, which will take years and billions of dollars to take root. There is no real alternative to poppy yet, the farmers claim.

No alternative? What, then, to make of a study by the French-based Senlis Council, which bravely proposes to introduce licensed opium production in Afghanistan for pharmaceutical painkillers? Senlis thinks this could be a panacea for a country that has in recent years depended on opium for about half of its GNP.

The council points to an alarming shortfall in the supply of painkillers, particularly in poor countries. Only 24% of the world's pain relief needs are being met currently, it says, while 77% of the world's morphine and codeine are consumed by just seven developed nations. It seems a particularly cruel irony that such drugs are almost unavailable in Afghanistan, the world's biggest producer of opiates, from which these medicines are derived.

For the Afghan government, with internal revenues of just $350m last year, the rewards from licensed pharmaceutical production could be huge. Senlis proposes a tightly regulated system of licensed farming, not as a substitute for the existing carrot and stick system of “alternative livelihood” schemes and eradication threats, but as a complement to them. It sounds neat, but the details are unrelentingly vague and the Afghan government and the UN are so far unimpressed. Both point to the fragile state of security in the country as the primary obstacle to administering any such scheme, at least for the time being. Countries currently producing legal opium include Australia, India, Turkey and France; none faces remotely the internal security problems of Afghanistan.

Corruption is rife within all Afghan government organs, and central authority is barely felt in the lawless south and south-west, where opium production rose several hundred percent in provinces such as Farah this year. In such circumstances it would be hard for the authorities to prevent legally-produced opium from being diverted into the illicit market—as long as the price for illicit, rather than pharmaceutical, dope remains far higher. The response from Senlis is that nothing can be worse than the current situation. And despite the 21% reduction this year, there is no doubt that the danger that Afghanistan will become a narco-state remains real.

While being politely careful to express their gratitude for a study that “offers an alternative option”, western officials are in private worried that the suggestion that opium production could be licit might confuse Afghan farmers. Last year's anti-opium campaign included the issuing of numerous *fatwas* against opium farmers on the understanding that production is *haram*—forbidden in Islam. The Afghan government's backers are presumably now hoping that the farmers do not take too much inspiration from Senlis as the new poppy planting season gets under way this month.

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Kirgizstan

Not a bed of tulips

Oct 6th 2005 | ALMATY
From The Economist print edition

Political violence after the revolution

SIX months after the “tulip revolution” that saw the overthrow of President Askar Akaev, Kirgizstan is still beset by political instability. The outraged reaction to the killing of Bayaman Erkinbaev, a prominent member of parliament and leading businessman, on September 21st—the second assassination of an MP since the revolution—has exposed a fierce struggle for dominance between the executive and the legislature. It was the charges of vote-rigging in the election of this body, in February and March, that sparked the uprising.

Parliament met in emergency session and passed a resolution declaring that the criminal situation in the country had “sharply deteriorated over the past several months” and that the work of the security services was unsatisfactory. It also called on Kurmanbek Bakiev, who became interim leader in March and was elected president in July, to sack several high-level officials. Some MPs further charged that corruption and criminal behaviour had increased on Mr Bakiev's watch.

The president, who attended the session, responded tartly that among the parliamentarians are businessmen who are often in conflict with the law, for anything from tax evasion to the bribing of law-enforcement agencies. His critics, however, note that the president has just sacked the procurator-general, Azimbek Beknazarov, who had doggedly pursued cases of corruption, some of them involving friends and relatives of the ousted president. Perhaps, they say, the procurator-general's sacking was meant to forestall too close a look at the current president and his team.

The tulip revolution does appear to be in trouble. Parliament has now demonstrated its lack of confidence in the country's security services by allowing members to carry firearms. It also blocked several ministerial nominations proposed by the president last week, notably the appointment as foreign minister of Roza Otunbaeva, a central figure of the revolution.

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Economist.com
WORLD
AFRICA & MIDDLE EAST

Southern Africa

From hand to mouth

Oct 6th 2005 | LILONGWE AND NSANJE
From The Economist print edition

Getty Images

Once again, southern Africa is facing a severe food crisis. It is a chronic problem—and shouldn't be

AT THE Trinity hospital in Malawi's southern Nsanje district, three-year-old Mboyi is lying listless, his face against the wall. His belly is badly bloated and skin is peeling off his legs. His mother explains that the family has not been able to harvest anything this year, due to poor rains. Mothers in the area are already bringing malnourished children to hospitals in alarming numbers. Yet it will be another six months before the next harvest.

Aid agencies are sounding the alarm, hoping that help will come before emaciated children's haunting images, such as those recently seen in Niger, appear on western television screens. The UN's World Food Programme (WFP) says that close to 12m people across southern Africa will need food aid before the next harvest. The agency is short of more than $150m to feed them over the next six months.

Malawi and Zimbabwe are by far the hungriest, but Mozambique, Zambia, Lesotho and Swaziland are also affected (see chart on next page). The drought may be southern Africa's worst in a decade. The crucial rains of January, when newly planted crops need water, did not come on time. Nor, in some places, did seeds and fertiliser. Maize, the staple food, is scarce in some areas; prices in markets have shot up beyond the means of the hungriest.

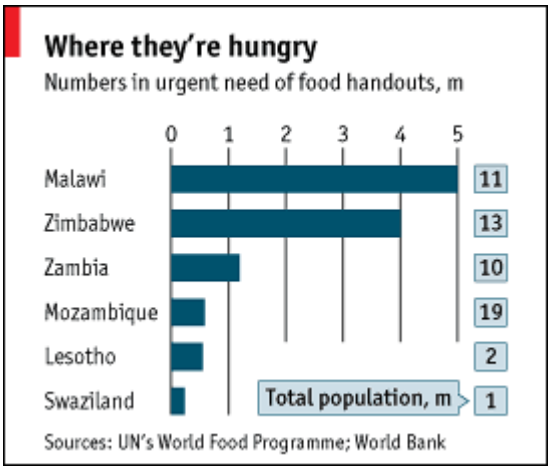
Though the problem is particularly severe this year, it recurs across southern Africa. Food is produced mainly by subsistence farmers on small plots with no irrigation, their fate tied to rain

falling in the right amount at the right time. Bad roads and unreliable transport make it expensive to move food and seeds. Without proper marketing channels, small farmers cannot sell whatever surplus they may have outside their neighbourhoods. This leaves southern Mozambicans hungry, even when crops are plentiful up north. Maize is ill suited to the climate, needing too much water. In Malawi, there are too many people for the land. Partly due to bad farming, yields are low. And the region has the world's highest rate of AIDS.

Many small farmers struggle to make ends meet even in good years, so one bad season can be disastrous. And in Swaziland and Mozambique they are facing their fourth dry year in a row. Unable to grow enough to feed themselves or borrow their way out of hard times, farmers end up losing the few assets they have. In Malawi, those without anything left often resort to cutting and selling firewood, further eroding the soil and making their plots still less productive, or else fishing already depleted waters. Others venture into crocodile-infested rivers to dig out water-lily tubas for food.

Bad government policy sometimes makes things worse. In Zimbabwe, once the region's breadbasket, land grabs have crippled commercial agriculture and irrigation systems. Hyperinflation and lack of foreign exchange make it hard to buy seeds and fertiliser, while fuel shortages stymie crop transport. A recent operation to “clean up” cities by bulldozing supposedly illegal dwellings has left another 700,000 people destitute, adding to the ranks of the hungry. The government has so far refused to endorse the UN's proposed emergency programme to help those affected.

Other governments are less bloody-minded. Malawi, the worst-hit country, with 5m people (nearly half its population) needing food handouts, wants help. In July, President Bingu wa Mutharika asked his compatriots to give to a “feed the nation” fund: so far, $565,000 has been collected. In August, the UN appealed for $88m. The World Bank will give $30m.



Harnessing what the region already has would go a long way to offsetting its chronic hunger. In southern Malawi, rivers regularly flood—and are badly managed. By contrast, a big sugar plantation in Nchalo, its sprinklers spitting out arcs of water, is a green oasis. On a smaller but no less hopeful scale, the nearby Chitsukwa irrigation scheme cost only about $20,000 and provided canals and enough low-tech pumps to water 18 hectares (45 acres), which sustain 176 farmers. Along the canal, women with babies on their backs labour on what look like portable stairmasters, pumping water into their fields: the maize is flourishing. Now armed with better knowledge, farmers are aiming at three crops a year, instead of the precarious single one to which they were accustomed. A few kilometres down the road, the land is hopelessly dry and barren.

Uladi Mussa, Malawi's minister for agriculture and food security, insists that expanding small-scale irrigation is a top priority. The potential is there, he explains, but Malawi lacks the know-how and money to do it on its own. Zambia and Mozambique have both welcomed exiled white Zimbabwean farmers, whose skills are already boosting local agriculture.

Meanwhile, chronic hunger is threatening southern Africa's future generations. Close to half of Malawi's under-five-year-olds are stunted. Schools unable to feed their pupils report drops in attendance, as children are too weak to walk or are forced to help their parents find food. For them, the damage will remain long after the rains have come.

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Economist.com WORLD AFRICA & MIDDLE EAST

Algeria

A flawed charter

Oct 6th 2005 | CAIRO
From The Economist print edition

Peace, generally; reconciliation, for some; truth and justice, no

Get article background

SOME Algerians say that Abdelaziz Bouteflika's presidential offering should be described as amnesia rather than an amnesty. He has presented his grandly-named Charter on Peace and National Reconciliation, which Algerians approved in a referendum last week, as the only way to turn the page on more than a decade of bloodshed in which some 150,000 people were killed. It may have that clement effect on many; but for many others it will not.

The charter grants a pardon to Islamist militants in prison, on the run and even those still fighting if they lay down their arms. No one will have to stand trial, even for murder, unless implicated in massacres, rapes and bombings in public places. Just as controversially, the document also shields the army and security forces from criticism over their dismal human-rights record and specifically from accusations of responsibility for the thousands of people who “disappeared” after being arrested. At least 6,000 have never come back; some put the figure at more than 10,000. The charter offers financial compensation to their families, but no promise to seek the truth about the disappearances.

Organisations representing the victims of terror and the families of the disappeared say that the charter is a denial of truth and justice. “We want the courts to deal with those who ordered and those who carried out acts of violence, even if Mr Bouteflika later pardons them,” said Cherifa Khaddar, head of Djazairouna, an association representing victims of terror. She and others say that one of the most galling outcomes of an earlier amnesty offered by the president has been the return of pardoned militants to their old neighbourhoods to live side by side with the families of those they killed.

Some Algerians say they would have preferred something like South Africa's Truth and Reconciliation Commission, where perpetrators of violence had to acknowledge their crimes without being punished for them. Those Algerians who campaigned against the charter found themselves silenced, excluded from the state media and even arrested.

But to many people in this exhausted country, eager to turn the page, the promise of peace and reconciliation has been hard to turn down. Official figures say that more than 97% of voters backed the charter on a turnout of 82%. Opposition parties say those figures are bogus and that turnout was no more than a quarter of what the government has claimed. Even so, of those who voted, a large majority probably did say yes.

Mr Bouteflika may hope for the amnesty to lure some of the few hundred militants left fighting in Algeria down from their hideouts in the mountains. But there have been no negotiations. The main militant outfit, the Salafist Group for Preaching and Combat, has rejected the offer.

Critics of the president say that those looking for surrender are missing the point. The amnesty's

main purpose, they argue, is to get impunity for the army generals who brought Mr Bouteflika to power in 1999. He has tightened his grip at their expense, slowly edging some of them out. Many believe that the price of their departure has been a guarantee that they would never be asked to account for abuses during the fight against the Islamists. It was after the main Islamist party had won the first round of a general election at the end of 1991 that the army stepped in, whereupon a brutal Islamist rebellion and a no less brutal counter-insurgency ensued.

Algeria is now largely at peace, but the generals will not have forgotten the calls at home and abroad in the late 1990s for an international investigation into the violence. The fate of the disappeared is still unexplained, as is the army's failure to prevent several large-scale massacres of villagers even though it was on the scene. And now that the charter has been approved, it will be harder than ever for such issues to be raised in Algeria's courts.

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Economist.com WORLD AFRICA & MIDDLE EAST

Namibia

Donkey business

Oct 6th 2005 | JOHANNESBURG
From The Economist print edition

A nice way to protect drivers—and donkeys

FORGET drunken driving. When cruising along Namibia's long and empty roads, unsuspecting drivers face a no less dangerous hazard: sleeping donkeys. At night, the warm tarmac provides a much more comfortable bed than the vast expanses of land only a few yards away. Invisible in the dark, the dormant asses, which help plough Namibia's land and pull its carts, have become a cause of many a car crash, to the dismay of drivers and the police alike. In May, the head of the president's guard was killed—by a donkey.

Russell Hay, a British businessman, is no stranger to asininity. While living in Namibia, he has twice driven into a donkey. On a lonely northern stretch, he swerved to avoid one, only to see it flattened by a lorry behind him.

Earlier this year, he and a friend set up Donkey Welfare of Namibia. With the Namibian government's blessing, the British outfit is planning to make donkeys glow in the dark by attaching reflective tags to their ears.

A pilot scheme is about to be started in two or three of Namibia's donkey hot spots. If it works, Donkey Welfare is thinking of enrolling local schools to tag the animals for a small fee—and British animal lovers may be asked to contribute. Donkey Welfare is also thinking of paying for donkeys and yellow carts, painted in the fashion of American school buses, to lug children to school. Namibia's 200,000-odd donkeys should be enough to do the job.

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Economist.com WORLD AFRICA & MIDDLE EAST

Palestine

Hamas hurt

Oct 6th 2005 | RAMALLAH
From The Economist print edition

For once, the main Islamist movement has lost ground. For how long?

LEST anyone doubt its commitment to both ballot and bullet, Hamas exercised both this week, bringing its gunmen and its voters on to the streets. On the eve of local elections, it admitted to kidnapping, blindfolding and killing an Israeli sweet-manufacturer. The night the election results were announced, its gunmen stormed a police station in Gaza city, killing its deputy chief.

How did this go down with the voters? In Beitouniya, scene of the sweet-maker's kidnapping, near the Palestinians' administrative capital, Ramallah, the campaign was livelier than ever—and Hamas's green bunting much in evidence. “Why should we cry over an intelligence operative, in a week when Israel killed one of our people every day?” said a bareheaded housewife as she cast what she called a sympathy vote for Hamas. Its candidates, drawn from the ranks of teachers, electricians and ironmongers, seemed to enjoy their day in the sun, after years of rule by the Mercedes elite of Fatah, the late Yasser Arafat's secular-minded ruling party, which has been struggling to impose its authority under a new leader, Mahmoud Abbas.

But if Hamas meant its salvo of home-made rockets to serve as a pre-election gesture to prove its heroism, it backfired. Of the 104 municipalities at stake in the third of four rounds of local elections, Hamas won just 13 outright, to Fatah's 51. Many it chose not contest; where it did, it won just over a quarter, far short of the 40% it expected. Fatah competed in more, and won outright in half. The fear of a Hamas triumph had induced Mr Abbas' ill-disciplined members to close ranks.

Election irregularities may have helped too. Registrars helped the illiterate and infirm sign in the box marked F for Fatah. The vote scheduled for the Gaza strip, where Hamas's constituency is strongest, was scrapped indefinitely. What with the commotion over Israel's evacuation, said the authorities, they had no time to prepare.

Hamas seems to have accepted this reversal, skewed or not, and did not cry foul at the results. For over a year, its political wing insisted that Hamas was putting politics above armed rebellion, and aspired to power through the ballot box in the delayed parliamentary election now due in January. Its last suicide bomb in Israel proper was over a year ago. It has largely kept a truce it agreed to in Cairo in March, and has signalled its readiness to extend it. “If the possibility of elections is real, we may then decide to continue the ceasefire,” said its spokesman, Mohammed Ghazal, a Brooklyn-educated vegetarian, shortly before the Israelis put him in jail. “I prefer peaceful ways.”

But Hamas's famed discipline now looks shakier. As a reminder of its durability, its hitherto secret military leadership went public last month. Its 5,000 well-armed militiamen promote a message that they, not a few hundred local councillors, are the instruments of liberation. Despite a promise not to parade their weapons in public, Hamas's armed men still roam Gaza's streets. In the past weekend, the security forces of the Fatah-run Palestinian Authority had their most violent clashes with Hamas for almost a decade.

Hamas's political wing also feels squeezed from outside. Its leading spokesmen, including Mr Ghazal, were among 400-plus Palestinians jailed in Israel's recent sweep of the West Bank. So too were a dozen candidates.

Diplomatically, Hamas's political wing is losing ground too. Before the mortars had landed, Ariel Sharon, Israel's prime minister, said he would obstruct Hamas' participation in the January election unless it recognised Israel and disarmed. America's secretary of state, Condoleezza Rice, warily voiced support for those objectives but proposed a timescale of years rather than months. “We do, I think, need to give the Palestinians some space to try and reconcile their national politics, but they're going to eventually have to disarm these groups,” she said.

Hamas's political plight may not, however, be good for peace. With local elections in Gaza deferred, it has already turned violent there again. In a taste of what may be in store if the general election is again postponed, some Hamas leaders are threatening civil war against the PA. “In politics,” said Mr Ghazal, “we have to compromise.” Outside, they don't.

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Djibouti

Qatnappers

Oct 6th 2005 | DJIBOUTI
From The Economist print edition

Try doing business without Djibouti's favourite drug getting in your way

MOST of Djibouti's men (and some women) spend their afternoons at home, in the streets or on the floor of their government offices, chewing fresh leaves and tender shoots of the plant, holding the mastication in their cheeks like golf balls, for hours on end. After midday, when the daily qat plane flies in from Ethiopia and Djiboutians start queueing to buy their fix, serious business meetings become impossible.

Chewing qat gives a similar high to adrenalin, making the consumer more talkative, alert and sociable. It also reduces the appetite. Long-distance lorry drivers, shepherds and guards have long used the leafy shrub to help them in their work—but be wary of the driver with that bulge in his cheek. That first effect eventually wears off, and the users become lethargic. Central Djibouti, in the afternoon, is a ghost town, gently decaying in the heat and dust.

Qat's drawbacks are many. Try finding a place to live: if the potential landlord is a regular chewer, all promises to clean the flat, install air-conditioning or even provide some simple furniture will probably come to nought. Residents of the tiny country, wedged between Ethiopia, Eritrea and Somalia, on the Red Sea coast, recall with a smile a short recent episode when the qat supply was interrupted. By the time the stuff was properly out of their system and the men had decided energetically to repaint their homes, supply was resumed and their ambitious plans were promptly shelved.

Still, qat can also oil the wheels of Djibouti's business. If you can stand its insipid taste and the ensuing thirst, chewing it with colleagues is a good way to bond, though it is mildly addictive and the long-term consequences may include heart disease, anxiety or even paranoia. On the plus side, some British researchers say it may increase male fertility, though it can also (Djibouti males deny this) destroy the male libido.

Djibouti's government is easy-going, with tales of bulging cheeks in the presidential garden. More tellingly, the distribution of qat is the economy's most efficient part. Small boats rush the stuff to towns at the other end of the coast. Other supplies, such as food and clothing, take the slow boat twice a week.

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Turkey and the EU

A chaotic start with pitfalls ahead

Oct 6th 2005
From The Economist print edition

AP

Keeping the EU's date with Turkey turned out to be a messy business

Get article background

IT WAS hardly the Union's finest moment, but the European gift for squabbling over details, and finessing deadlines, was shown off to good effect. In the small hours of October 4th, the British, who hold the EU's presidency, claimed to have kept the Union's promise to launch membership talks with Turkey—on precisely the agreed date, October 3rd.

It was all a matter of which time zone you were in, the Brits explained. If you went by Greenwich Mean Time, the appointed day was still in progress; never mind that in Luxembourg, where the talks were in progress, it was two hours later, and in Ankara yet another hour on. And anyway, chimed in Olli Rehn, the European Union's commissioner for enlargement, we could always have "stopped the clock" for a few hours if necessary.

Interrupting the march of time is probably not the most difficult thing that Turkey and the European Union will have to do if the promise of full Turkish membership is to become reality, presumably in a decade or more's time. But the British achievement, in sorting out all the last-minute problems over talks with Turkey, was still significant. It showed that the Union is still capable of taking hard decisions, even after its leaders declared their whole project to be in crisis after a pet initiative—the approval of a European constitution—virtually collapsed during the summer.

But the huge difficulties of getting to the starting-point with Turkey suggest that the country's Euro-troubles have only just begun. So awkward was the haggling that Britain, whose turn it was

to chair the talks, kept the terms of the final compromise hidden from most of its European partners until Turkey's prime minister, Recep Tayyip Erdogan, had signed on the dotted line. That in turn cleared the way for his foreign minister, Abdullah Gul, to set out from Ankara to Luxembourg. Only at a late-ish stage did Britain present the deal to its partners, congratulating them all on their fine diplomatic achievement. Others, dismayed by this sleight-of-hand, were left muttering darkly about Albion's perfidious tactics.

The Turks must now turn to the tougher problem of actually getting in. This means, first, fulfilling the normal conditions of entry, including adopting over 80,000 pages of EU law. These are divided into 35 so-called “chapters”, each covering a topic such as justice and home affairs. All 25 EU members must agree that Turkey has met every condition in each chapter for that bit of the negotiation to be closed. In other words, anyone can hold up talks at any time. The Greek-Cypriot president, Tassos Papadopoulos, has assured his voters that he has scores of vetoes up his sleeve.

Indeed, the summit in Luxembourg also showed that Turkish entry into the EU will be inconceivable unless Cyprus is solved. That problem resurfaced because the EU's entry terms require newcomers to align their foreign policies with the EU in international bodies. In the final stages of the talks Turkey grew worried about this: it voiced the fear that if it joined the Union, it could not veto any application by the Greek-Cypriot government to join NATO.

In fact, its worries were excessive. All the same, it required phone calls from Condoleezza Rice, America's secretary of state, to the Cypriot president (getting assurances that Cyprus does not want to apply) and to the Turkish prime minister (saying don't panic) to allay the fears. The need to call in the Americans, who a month ago were being told to keep out of the EU's talks with Turkey, is a worrying portent for the Europeans' ability to solve the Cypriot conundrum without transatlantic help.

Lastly, the Turks must prepare European public opinion for their entry. Both France and Austria have promised referendums and, at the moment, public opinion in those countries is overwhelmingly hostile. Earlier this year, the German chancellor, who supports Turkey's wish to join, said its attitudes to human rights were “incompatible with [the EU's] common values”. After the agreement, France's President Jacques Chirac said Turkey needed a “cultural revolution” to get in.

Yet whatever happens later, the decision to open talks has already had one important effect. It has kept the door open to further enlargement of the EU in the Balkans. Just 45 minutes after the start of negotiations with Turkey, the Union began accession talks with Croatia. The British said this was coincidence, but few people believed this.

Croatia's entry process broke down because of EU demands that it hand over a suspected war criminal. A sudden breakthrough came because Croatia had supposedly changed its ways, and Carla Del Ponte, the head prosecutor of the tribunal for war crimes, was able to report that Zagreb's authorities were “co-operating fully” with her. Perhaps. But her report appeared just as Austria's objections to Turkish accession talks were melting away—and Austria has been a strong backer of Croatian membership. To many Europeans, swallowing Croatia looks like the price of Turkish accession.

Whatever the truth of that suspicion, the decision to open talks with both countries should, European officials hope, forestall a new crisis in the Balkans. Many reckon that the hope of eventual membership of the EU is the only thing keeping the region's rickety states minimally stable. And their big fear was that, if both the EU constitution and Turkey were rejected, this aspiration would vanish and the region could slide into conflict once more.

If they are right, the EU avoided three crises this week: in Brussels, Ankara—and the Balkans. But

only just.

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Economist.com WORLD EUROPE

Turkey and Armenia

Even we wish you well

Oct 6th 2005 | YEREVAN
From The Economist print edition

Armenians back Turkey's hopes for a European future

Get article background

IF THERE was a country in the world that wished the Turks ill, you might think it would be Armenia, where most citizens say their people suffered genocide at the hand of the Ottomans in 1915—and wish Turkey would admit this. But in fact, Armenians cautiously welcome their neighbour's Euro-success.

Armenia's problems with the Turks are not just historical. Since 1993, the Ankara authorities have sealed the Turkish-Armenian border, in solidarity with their kin in Azerbaijan, part of whose territory is occupied by Armenians.

But people in the Armenian capital, Yerevan, assume that joining Europe will make Turkey change its ways: both its view of history, and its treatment of its neighbours. And the city's weary residents feel they need a break from tough regional realities. An isolated Armenia has had to find partners wherever it can. From Moscow to Los Angeles, the diaspora sends remittances; America's government also gives aid—$75m this year. But for ordinary people, life is hard.

The economy has grown on paper but produces little. In what was once a medium-sized Soviet city, the centre is full of craters where mass housing has been torn down to make flats for rich exiles. In the words of a foreign-ministry adviser, “there is no alternative to getting on with our neighbours.”

Arsen Ghazaryan, who co-chairs an association of Turkish and Armenian businessmen, is frustrated by the blockade. Braving the cost of transit through Georgia or Iran, he says, Turkish businessmen do around $100m worth of trade with Armenia annually. Every summer, thousands of Armenians catch the rays on Turkish beaches. But Mr Ghazaryan thinks of what might be: with its deep ports and vibrant internal market, he sees Turkey as a natural partner.

In their attitude to Turkey, there are differences between local and overseas Armenians. While Armenia's government hails Turkey's breakthrough, many in the diaspora called it an undeserved reward for an unrepentant nation. “It's easy to be principled in the diaspora,” retorts a young woman in Yerevan. “They don't have to live between Turkey and Azerbaijan.”

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Economist.com WORLD EUROPE

Kosovo's status

The wheels grind on

Oct 6th 2005 | PRISTINA
From The Economist print edition

A “frank” report clears the way for negotiations on Kosovo's future

Get article background

ON OCTOBER 4th, a long-awaited report on the status of Kosovo was handed to Kofi Annan, the UN secretary-general. By December, UN-sponsored talks are expected to start on the future of a territory which is still bitterly contested between ethnic Serbs and Albanians. With most observers expecting the talks to lead to Kosovo's independence, there is, or at least there should be, a sense of history being made; in the words of the province's UN boss, a “moment of truth” is looming. But the political mood in Pristina, the province's tawdry capital, is more sullen than jubilant.

Kosovo has been administered by the UN since fighting ended in 1999, though officially it remains linked to Serbia. Almost all its ethnic Albanian population—over 90% of the total—want independence, but Serbia refuses to agree. In the past few years, the UN has ceded some power to a local assembly, which most Serb politicians boycott. Most Kosovo Serbs still live in enclaves, some of which have to be protected by foreign peacekeepers.

The report—described by aides to its Norwegian author, Kai Eide, as a “very frank piece of paper”—will excoriate Albanian leaders for failing to protect Serbs and other minorities, and Serb politicians for refusing to act constructively in Kosovo's politics. It is also expected to recommend that talks on Kosovo's future status begin as soon as possible.

The man tipped to lead the negotiations is Martti Ahtisaari, a former Finnish president. After a round of shuttle diplomacy, he will probably draft a document on the province's future status which will then be put to Serb and Albanian leaders for consideration.

Until a few months ago, Serb officials were wildly unrealistic in their demands; they are now inching towards reality, although they are still not quite there. They now say that as long as Serbia retains sovereignty over Kosovo, and that its Serbs have autonomous areas, the province can be otherwise self-governed. In practice, they may have to concede quite a lot more than that.

Meanwhile, Kosovo's Albanian leaders are in disarray, perhaps underestimating the rearguard action that the Serbs may mount to stop the province seceding.The record of the local government is weak and it suffers from a whiff of scandal; also its president, Ibrahim Rugova, is gravely ill with lung cancer.

Against this unpromising background, most diplomats in Pristina reckon the territory is heading for “conditional independence”. This would mean Kosovo being fully self-governing, and endowed with some trappings of independence, like a seat at the UN, yet with certain limits on its elected authorities. That would create a situation similar to Bosnia, whose international overlord is entitled to fire any local leader who breaks the terms of the Dayton peace settlement.

Yet even with those provisos, it is hard to imagine Kosovo Serbs and Albanians agreeing on their

province's future status. According to one plausible scenario, the Serbs will refuse to negotiate any agreement leading to Kosovo's independence; but the UN security council may impose this anyway. On the Albanian side, an increasingly loud voice is that of a former student leader, Albin Kurti, who wants instant independence and mass protests against the looming negotiations. Much of Kosovo is decorated with his slogan: “No negotiations. Self-determination!”

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Spain's rowdy regions

Fudge or death

Oct 6th 2005 | BARCELONA
From The Economist print edition

Catalonia's bid for freedom will hardly go all the way

DESPITE their people's dour and thrifty reputation, Catalan politicians are excited by one thing—autonomy. So passions ran high in Barcelona's regional assembly last week, after it passed a constitutional statute that, if approved by the government in Madrid, would grant Catalonia an independent legal system and the right to raise taxes and to be called “a nation”. Pasqual Maragall, the region's mustachioed Socialist premier, was triumphant over the 120-15 vote in favour: “We will win and our people will celebrate.” His coalition partner, Josep Lluís Carod-Rovira, head of the nationalist Catalan Republican Left (ERC), was even more upbeat—declaring a new dawn for Catalonia.

On no count is this optimism likely to be proved right. But the vote has put José Luis Rodríguez Zapatero, Spain's left-wing prime minister, in a bind: while he can hardly approve a measure which, on the face of it, clears the way for possible Catalan independence, his government depends on support from leftist Catalan nationalists. He has therefore promised not to reject the statute, so long as it is toned down. The opposition People's Party (PP) has already rejected it outright. As for Mr Maragall's claim of “celebration”, a survey suggested that only 4% of Catalans felt the statute to be important.

Given that the initiative seems so doomed, this may be unsurprising. And, indeed, Catalonia already has a high degree of autonomy. The PP fears that granting it any more would provide encouragement to Spain's other querulous regions, especially the Basque one. There is force in that argument. Earlier this year, the nationalist Basque government's bid to define its relations with the centre as “free association” was foiled by legislators in Madrid. Meanwhile, the Valencia region's PP-run government has rocked the boat by voting to call itself a “historic nation”.

A parliamentary commission will examine the Catalan statute in November, though it will probably not be voted on in Madrid for a year. A compromise is likely—as closer inspection of the text suggests. It is ambiguous on how the province would levy taxes, prompting suspicions that the central government may retain some control over the regional tax-raising body that could now be established. With a fudge like that, rowdy Catalan politicians could claim victory, without the centre having yielded a jot more power to the province, and all the parties would be happy. At least, until the next region comes up with a similarly cheeky proposal.

Polish education

Time for the tricks to stop

Oct 6th 2005
From The Economist print edition

Dishonesty is endemic in Polish education

SITTING among the pigeons of Cracow's market square, six “students” struggle to complete the final high-school exam. One by one, they are caught cheating, and forced to stand up, showing their masks: well-known corrupt politicians and businessmen. This pointed little street drama was organised by Law and Justice, the party that won Poland's recent elections.

The equating of corruption with cheating is a new idea in Poland. People rage over corruption, but mostly see cheating in exams as no more of a moral question than disobeying traffic rules. Cheating equipment is a thriving business. One favourite is a pen that writes in ink visible only under an ultra-violet light (which is cunningly concealed at the end of the pen). So seemingly blank sheets of paper can contain crucial notes. A cruder pen, slightly fatter than normal, contains a long, spring-loaded scroll of paper. Over 9,000 of these were sold in September alone. Educational publishers turn out “revision guides”—complete with versions in tiny type, easy to tuck up sleeves or into belts.

And there isn't much moral questioning from the book trade. “It doesn't bother me at all that we sell these booklets. Though if I had children, I wouldn't let them cheat,” says Tatiana Druszcz, a manager at EMPiK, a Warsaw bookstore.

Cheating is entrenched in Polish educational culture, far more than in other post-communist countries. One reason is general admiration for all forms of dissent, ingrained in a society with long memories of foreign-imposed rule. But those days are gone. Cheating looks out of place in a country that prides itself on high educational standards. The authorities have been moving in the right direction by overhauling the high-school final exam. High grades in that test used to translate into perks for teachers, with predictable results. This year, for the first time, core subjects were graded externally, with visiting teachers present in the exam rooms. The education ministry said students caught cheating would fail—though they could resit the exam later.

But the real sign of change could be linguistic. The word for cheating—*sciaganie*—suggests ingenuity, not dishonesty. Only when Poles find a more pejorative term will this dubious habit lose its moral immunity.

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French unions

Sound and fury, signifying little

Oct 6th 2005 | PARIS
From The Economist print edition

Reuters

A loud bark, a softening bite

Some labour protests are more spectacular than effective

Get article background

NOW and again, French reality can surpass the wildest imaginings of fiction. The nation has just lived through ten days that felt like a series of scenes from a poorly-made B-movie: a hijacked ferry, a helicopter rescue mission, abseiling commandos, balaclava-clad rioters, and at least 1m people taking to the streets to chant angry slogans and let off steam. The common theme in all these events is union-led protest—against privatisation, the lack of job security and low wages. But behind the theatrics, measuring the real ability of the trade unions to influence events is somewhat more difficult.

Two separate protests underlie the recent wave of eye-catching dramas. One is over the future of SNCM, a loss-making state ferry fleet which links the island of Corsica with the French mainland. In mid-September, when it emerged that the government planned to sell the whole company, unions reacted angrily. They blockaded ports, briefly kidnapped the company's boss, seized a ferry and then set sail from Marseilles. In a ten-minute raid, commandos retook the ferry. Despite a government promise to keep 25% of the firm, protests and blockades spread to Corsica's ports, such as Ajaccio and Bastia: thousands of bewildered travellers were stranded, and riot police were called in to get the ships going.

This week's one-day strike was a separate fixture, which had been planned a long time in advance. All France's unions, backed by the opposition Socialists, voiced a whole series of grievances—over new labour laws, privatisation and the erosion of living standards. Between 450,000 and 1m people took to the streets in scores of towns across the country; public transport was disrupted; some schools closed. Bernard Thibault, head of the Communist-backed General Labour Confederation (CGT), the biggest union, boasted afterwards that the day of discontent had been “undoubtedly a great success”.

It depends, of course, on how you define success. This sort of drama can certainly grab headlines and dent France's international image—but does it get results? On SNCM, it is true the government has already given some significant ground. It has raised to 34% the share that it suggests should be retained by the state and employees combined. This joint holding would amount to a blocking minority share, so the government's concession is more than a token one.

While the authorities have threatened to let the company sink if no deal is done, nobody believes they would actually dare to do so. The government's emollient behaviour can partly be explained by fears of stirring up local nationalism as well as labour unrest. Anything to do with Corsica, with its history of fiery and occasionally violent separatism, is always treated as a special case. The latest troubles have stirred the island's passions, blurring the line between anti-French and anti-privatisation protests. In view of the Corsican factor, yielding over SNCM does not necessarily imply that the government will go soft on other fronts.

The one-day national strike was a clearer test of the government's will-power. Dominique de Villepin, the prime minister, said he “heard” the protesters' message. Yet he has no plan to alter the new job contract, which enables firms employing fewer than 20 people to shed workers more easily over the first two years of their existence. This is a boon to small businesses, but it was an enormous gripe for this week's demonstrators, who are dismayed by an increasing liberalisation of the labour market, and a sense that the old days of legally-enforced job protection may be going for good.

Apart from help with the cost of long car journeys to work, no immediate moves are planned to ease the cost of living. Nor has Mr de Villepin followed up on one particularly daft, populist proposal that he floated recently. He said he might try to force Hewlett-Packard, an American computer company, to pay back subsidies that it had supposedly received from the state. His gesture was a sop to trade unionists, who—to judge by the slogans heard this week—are particularly incensed by redundancies at that American firm. But on closer inspection, it has turned out the computer firm received no help from the government in Paris, and the matter has been allowed to drop quietly.

Moreover, aside from SNCM, the government is pressing ahead with its privatisation plans. It sold a stake in Gaz de France, the gas utility, earlier this year; it is privatising motorways; and it plans a share offer for part of EDF, the state-owned electricity company.

Judging by results achieved rather than noise created, France's unions are waning. Over the past two years, protests and strikes did not manage to prevent a state pension reform, and a mini-reform of public health-insurance. This failure reflects government tactics (dividing the unions), new rules (like docking pay for public-sector strikes) and success in negotiations (which have secured a basic public transport service during strikes). If unions still have a loud voice, it is not because of their mass membership—only 10% of French workers are unionised, against 13% in America, according to figures from the OECD—but because they co-manage unemployment and health-insurance funds.

So can the government afford to dismiss the latest demonstrations as an autumn ritual? Not without incurring some political risk. In 1995, a centre-right government led by Alain Juppé was fatally wounded by paralysing national strikes. And charges of political deafness can sting. But perhaps the more important point is that with unions on the back foot, there could be more room for reform in France than pusillanimous politicians think.

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Charlemagne

A few more smiles wouldn't hurt

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The EU's leaders needn't always look so gloomy

MOST governments hype success and hide failure. A few even try to celebrate their failures, in the hope they will look like successes. But these days, Europeans are pioneering the opposite approach: sexing down their achievements.

The expansion of the European Union has been a triumph, bringing stability, modernisation and prosperity to new members and old. If Turkey were to join the club, both sides could get those benefits and more—the geopolitical advantage that comes from treating a moderate Islamic country as one of your own. Considering Turkey has waited decades for this moment, and considering there have been several embarrassing setbacks for the Union this year, it might have been reasonable to expect a little celebration on the day those Turkish talks started.

Yet reactions were muted. The British foreign secretary's speech, opening the first session, mixed brief words of welcome with hectoring Turkey for its problems and agonising about how difficult the negotiations will be (and they will). The talks before the talks were not exactly a lap of honour, either. The next day, the presidents of the EU and France went out of their way to point out, helpfully, that accession talks might fail. People seemed determined to accentuate the negative.

It is fair to point out that there were no fireworks over the Bosporus, either: after all the bad-tempered haggling, Turks were not in a mood to rejoice. But for European leaders, this downbeat reaction is part of a pattern: they often react morosely to success.

Exhibit A is the whole process of economic reform. True, European economies are in trouble and unemployment is high. But with the big exception of Germany, joblessness is considerably lower than it was in the late 1990s. In the past decade, the EU, admittedly with a larger population, has created as many jobs as more dynamic America. But you would never know this from politicians,

who seem to believe endlessly high unemployment is the cost Europeans have to pay for a civilised way of life.

And the main reason why unemployment has come down is that, in fact, many countries have adopted labour-market, pension and other liberalising reforms in the past few years, and are now reaping the benefits. But you would never know this either, because leaders, at least in public, swear blind they will never allow “hyper-liberal” reforms in their country, or that, if they must, they will swallow the medicine only because someone else—usually the hard-hearted European Commission—insists.

There is one understandable reason why politicians are taking this approach: many voters seem adamantly opposed to what they are doing. Three-quarters of Austrians, for example, object to Turkish accession. And it is right that elected politicians reflect public opinion. But, as Edmund Burke said, leaders have another duty—to give voters the benefit of their best judgement. And you can hardly expect the public to muster enthusiasm for a project when their leaders are ambivalent or pessimistic.

The same applies to recent trends in eastern Europe, where there is lots of good news for anyone who cares to notice. The fact that many ex-communist economies are now showing flexibility and rapid growth is of huge benefit to the whole of Europe; but few leaders in old Europe point this out. As a result, populist grumbles prevail; Polish plumbers turn into bogeymen, posing a supposedly fearful threat to western Europeans.

European leaders are often equally oblivious to the benefits of things the public likes, or at least doesn't oppose. One of the few areas where the EU can match America in global influence is world trade. Europeans have benefited greatly from the trade openings that the EU has (more or less consistently) encouraged.

Most people, when asked, say they oppose protectionism and therefore like it when the EU uses its influence to boost freer trade flows. But that didn't stop Jacques Chirac attacking the EU's trade liberals this week, by claiming they had failed to protect European jobs during the Doha round of talks.

Time to count some blessings

Given their track record, politicians can't shift the responsibility for not celebrating success onto a risk-averse public. On this matter, the fault, dear Brutus, lies not in our stars, but in ourselves: that's what they would admit if they were more honest.

Of course, one can appreciate some reasons why Euro-politicians hesitate to look on the bright side. They have been traumatised by recent setbacks: first, the stunning blow of the constitution's rejection by French and Dutch voters; second, the less momentous, but still frustrating, failure to agree on an EU budget for the years 2007 to 2013. European leaders have rarely been as pessimistic about the Union as they are now. They have suffered a crisis of confidence. And this crisis affects not only projects that are rightly controversial, like the constitution, but also success stories like enlargement.

But if the crisis of confidence is understandable, it is still damaging. It risks reinforcing one of the biggest failures of European policy, that of economic reform. The problem is not that countries have failed to reform at all; it is that changes have been partial and piecemeal. France, for example, reformed its pension system—a step forward. It imposed a 35-hour week—a step back. Belgium tried to increase companies' demand for labour through corporate tax cuts; the benefits were promptly captured by existing workers through pay rises. Germany's reform plans have been

stop-start affairs. This incoherence is directly related to politicians' failure to have the courage of their convictions. Reform works wherever it is tried, but because nobody dares say so, it has not been tried much. Europeans are in danger of talking themselves into a state of inertia.

The moral of the story is not “don't worry, be happy.” But politicians should at least take credit where it is due. Things are difficult enough in Europe without making a crisis out of the opportunities and successes that do come along.

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Conservative leadership election

The line-up

Oct 6th 2005 | BLACKPOOL
From The Economist print edition

What the Tory party conference revealed about the next leader of the opposition

Get article background

STILL smarting from a third electoral defeat, Conservatives gathered in sullen mood this week in Blackpool—hardly the most inspiring place to contemplate renewal. Party members knew they had a week of auditions to sit through for the role of leader of the party, and that most of the candidates would tell them that they had to change, or die.

For many, death seemed preferable. Fully 44% of people identifying themselves as Tory voters told a Populus poll for the *Times* that Britain would be better off if the Conservatives were replaced by a new right-of-centre party, an increase of 15 percentage points on this time last year.

Which makes it odd that this year's conference turned out to be optimistic and energetic—exciting, even. The speeches of the five candidates to be the party's next leader breathed a whiff of revival into the hall. They even gave depressed Tories an inkling that they might at last have the beginnings of a winning team.

This was partly because the party was honest with itself about the terrible mess it is in. Things that Tory MPs at previous, more conspiratorial conferences have muttered in the safety of bars and restaurants—that their party often sounds selfish, parochial and bemused by contemporary Britain—this year came direct from the rostrum. Francis Maude, the Tory chairman, unencumbered by the need to pay lip-service to an existing leader, declared that the Conservatives “have no God-given right to survive, let alone to succeed”.

That was as self-sacrificing as it was brave. Mr Maude's unpitying honesty was greeted with predictable hostility by the chintzy ballroom of the Winter Gardens. But it cleared the air, enabling the leadership contenders who followed to sparkle and fizz with optimism, without first needing to make their audience feel like losers.

Two of the candidates—Ken Clarke, a former chancellor, and David Cameron, the shadow education minister—accomplished this masterfully. David Davis, the shadow home secretary, who began the week as the clear favourite, with many more pledges of support from MPs than any other candidate, was by contrast uninspiring (see article).

Being leader of the opposition is a difficult job that comes with high expectations and meagre resources. Incumbents must perform well from their first day and can quickly suffer a terminal loss of support if they stumble. It is now clear how Mr Clarke and Mr Cameron would go about the job, less so how Mr Davis would.

Mr Cameron spoke without notes and strode easily around the platform. With good timing, furrowed brow and a nice line in sincerity, he invited comparisons to Tony Blair—a compliment even among Conservatives these days. Away from the main stage, the man who sells himself on

having the best understanding of Mr Blair's appeal talked about carrying Blairite reforms to the public services further than the prime minister ever could.

Members liked what they heard, though some also confessed they found it hard to recall afterwards precisely what it was that Mr Cameron had said. That didn't matter much in the canteen of the Winter Gardens. “He really lit them up,” reckoned an American observer from the Republican Party, which could teach the Tories a thing or two about winning elections. Mr Cameron picked up endorsements from MPs too, including that of Alan Duncan, shadow transport secretary, who had been leaning towards Mr Davis.

Mr Clarke chose a different line of attack. He focused on Gordon Brown's economic record and ridiculed New Labour's political culture. The speech was peppered with ebullient jokes at Labour's expense—with Mr Blair wrangling over when to pass the baton to Mr Brown, he “would not put those two in a relay team”. Mr Clarke created a sense that Mr Brown could be vulnerable, something that Mr Cameron almost managed (he called him “the great complicator”) but Mr Davis, lamely labelling him an old socialist, did not.

Apart from at one rare appearance at a fringe meeting, Mr Clarke avoided mention of Brussels or Baghdad, where his views are at odds with those of most Tory MPs. Some thought Mr Clarke's pitch dwelt too much on past success and not enough on what Britain would be like in ten or 20 years' time. But most forgave him that when he delivered his final line: “We search for leaders who will be seen by the public as prime ministers in waiting,” he said. “And boy have you kept me waiting.” It could have sounded terrible, but by then Mr Clarke had convinced party members that he could draw blood if they let him at Labour's front bench, and they laughed and applauded.

And what would Mr Davis offer as leader of the opposition? His platform speech inspired representatives less than those of his rivals: he was eclipsed by both Sir Malcolm Rifkind and Liam Fox, whose flag-waving, aimed squarely at the bit of the party that ought to belong to Mr Davis, kept alive his campaign. The front-runner had behaved all week as if he was the next leader and his campaign had gone well, despite being photographed with a couple of blondes in T-shirts with “It's DD for me” emblazoned across their breasts. After his set-piece, Davis supporters changed their tone: their man had spoken marvellously, they said, but had fallen prey to nasty journalists looking for an upset.

The content of Mr Davis's various speeches was patchy—a list touching on Tory totems, such as prisons, Europe and binge-drinking, that failed to sound fresh on any. At fringe meetings he dodged big issues such as pension reform, declared that the Tory's cranky immigration policy should stay and pledged that a main aim would be repatriating powers from Brussels, suggesting that he has not overcome his party's obsession with Europe.

Tory MPs know how ruthless Labour has proved at exploiting woolly thinking. Now more have doubts about how Mr Davis might perform under pressure. The excitement in Blackpool was the rush of blood when you know a race is on.

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Food labelling

Sea change

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British fish is starting to go green

DOVER SOLE with a squeeze of lemon is a British favourite—so much so that numbers in some parts of the English Channel have fallen dramatically since peaking a quarter of a century ago. But now fish lovers can tuck in without guilt—as long as the fish comes from Hastings.

The Marine Stewardship Council (MSC) this week certified two fisheries near the south-coast port—for herring and mackerel as well as Dover sole. The fisheries, it says, are managed so that their fish can be caught indefinitely without much harm to supporting species. The idea is to allow consumers to avoid fish grabbed from the sea without regard for what's left. Everything from fresh fish to pâté can be eco-labelled.

Rupert Howes, MSC's chief executive, knows his scheme cannot alone solve fishing's problem—which is that fishermen with bills to pay catch too many fish and politicians fail to stand up to them. But labelling does provide a mechanism for consumers to add their voices to calls for better fisheries management.

Although the MSC is based in London, its ambitions are global. White fish—a worldwide commodity for pies and breaded products—face strong competition for market share. When hokey was certified, South Africa certified its hake fishery, too, mindful of access to the US market. Now the Alaskan pollock fishery has done exactly the same.

In its five years, the MSC has certified 14 of the world's fisheries, six of them in Britain. MSC's labels are starting to appear in British supermarkets such as J. Sainsbury, Waitrose and Tesco. More international certifications are in the pipeline. But MSC has a long way to go, as its green fish are only 4% of the world's edible wild-capture fisheries.

Yet, it is a start. In the gloomy early days, there was no market for green fish because there was no supply, and no supply because there was no market. Unilever, whose frozen food contains lots of white fish, is to make eco-labelled fish around 30% of the total in Europe by volume, from less than 5% now. There will be nothing fishy about its origins.

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Economist.com WORLD EUROPE

Social mobility

Land of hope and glory

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From The Economist print edition

Why Britain is becoming less socially mobile

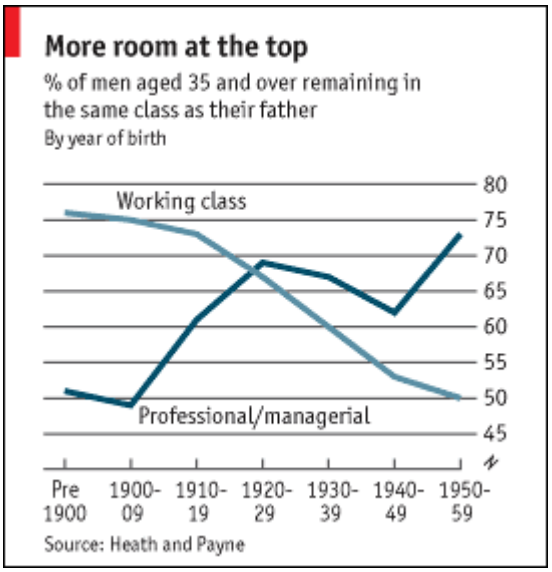
AMONG the stars of this week's Conservative Party conference were two men from starkly different backgrounds. David Cameron is the son of a stockbroker; he went to Eton College and Oxford University and is married to the daughter of a baronet. David Davis was raised by a single mother, lived for a time in public housing and attended the less prestigious Warwick University. That two men with such divergent “back stories” could both compete for one of the top jobs in politics—if leadership of the Conservative Party can fairly be described as such—suggests Britain is a land of opportunity. Yet, oddly, both men insist there is less social mobility than there used to be.

Government ministers and some academics agree. Earlier this year, a team of economists showed that people born in 1970 were less likely to have escaped their class origins than those born 12 years earlier. Mobility is likely to slow further in future, they claimed. Influential thinkers within the government have considered trying to do something about the ossification of British society, although they became less keen when it was pointed out that this might mean forcing some people down the social ladder as well as encouraging others to rise.

Are politicians right to worry about the decline of social mobility? Not really; nor is it conceivable they will be able to do anything about it. Britons are indeed more stuck in their classes these days, but the reason for this is nothing more sinister than economic progress.

In the second half of the 20th century, and especially between the 1960s and the 1980s, Britain's economy was transformed. The steep decline of manufacturing, alongside primary industries such as farming and coal mining, meant there was simply less manual work to go around. At the same time, white-collar jobs, particularly in business and finance, multiplied rapidly. Women flooded into the workplace, displacing men from mundane clerical jobs.

Anthony Heath and Clive Payne of Oxford University have used political surveys to reveal the effect of these changes on Britain's class structure. Roughly three-quarters of men born to proletarian fathers in the late 19th and early 20th century ended up working with their hands. But a similar boy born in the middle of the 20th century was just as likely to have pushed his way into a higher class by the age of 35 (see chart). Many were simply sucked into the expanding professional class. The trajectory of Mr Davis, who was born in 1948, was a common one.



This was, says Mr Heath, “a once-and-for-all transformation”, which has, inevitably, slowed in the last decade. Women have probably penetrated about as far into the job market as they will go: since the early 1990s, their economic activity rate has risen only slightly. Farming and manufacturing continue to decline, but more slowly than before. Now that they employ just one worker in eight, a mass exodus is scarcely possible. That is the main reason social mobility is slowing.

Another reason is that the upper middle classes have held their own. The proliferation of professional jobs meant the children of the well-to-do found it easy to follow in their parents' footsteps. Three-quarters of boys born to professional fathers in the 1950s ended up in the same kinds of jobs, meaning they had as much inertia as manual workers in the early 20th century. And, because the middle class has expanded, it can supply a large part of the white-collar workforce. As a result, there are now more David Camerons.

That does not mean Britain is becoming less meritocratic. More subtle changes are afoot. Consider, for example, the transformation of the financial-services industry. Before the 1980s the City was home to well-heeled but not especially bright folk who traded on their connections. Many were swept away by a bundle of reforms introduced in 1986, and for a while the “barrow boy”, a trader from humble origins, was in the ascendant. These days, though, more sophisticated markets demand computer whizzes and the highly educated—many of whom come from privileged backgrounds. Men and women with fruity accents are still found in the industry, but now they have MBAs.

The affluent used to have connections; now they enjoy educational advantages, which turn out to be just as useful. But, even if they prove dull, a fall into poverty is unlikely. Another trend in the past few years has been the growth of jobs that demand good breeding rather than good exam results. As John Goldthorpe, another Oxford sociologist, puts it, “Tim Nice-But-Dim doesn't end up on the shop floor. He becomes an estate agent.”

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Aberdeen

The price of oil

Oct 6th 2005 | ABERDEEN
From The Economist print edition

The city is booming but grumpy

OIL prices of more than $60 a barrel are a blessing for Aberdeen, self-styled oil capital of Europe, however much they harm Britain. Earlier this year the government issued a record 152 exploration licences. A quarter of the 99 applicants were new to the North Sea. There is plenty of excitement onshore, too. Aberdeen's streets are lined with expensive cars; unemployment is a mere 1.6%; and average weekly earnings in 2004 were £539, more than 6% above the British average.

Even so, the city's chamber of commerce and the oil industry are unhappy. Yes, says Geoff Runcie, the chamber's chief executive, dear oil is “great news” for his city. But in this business success is rarely permanent: everyone knows a price bust is as sure as the first winter storm. Worse, Aberdeen is paying the price of prosperity—and Edinburgh and London have only belatedly done anything to help.

Aberdeen suffers from poor road and rail links to the rest of the country. Eddie Anderson, of ARR Craib Transport, says that at rush hour it can take an hour to travel five miles: “When you are trying to do just-in-time deliveries to the docks, it adds enormously to the cost.” This is the result of underinvestment in the 1980s and 1990s, when the government converted the main road south into a dual carriageway, but did little else.

At that time oil was making Aberdeen rich, while the collapse of old industries was impoverishing the rest of Scotland. Aberdeen lost government spending and regional aid, much of it from the European Union. It went to central Scotland, as politicians sought to create jobs by luring foreign investment with the promise of subsidies and infrastructure.

The grievance is all the sharper because the Aberdonians' hard work was generating the oil-tax revenues that paid for much of the spending elsewhere. Even devolution in 1999 did not make much difference. The result is distrust of politicians in Edinburgh as well as those foreigners in London. Aberdeen has never had much enthusiasm for the Scottish National Party.

After decades of campaigning, the Scottish Executive has now agreed to pay for a £120m by-pass. It will also improve commuter services on the one rail line through the city. But Mr Runcie and his colleagues want more. Aberdeen's prosperity, they say, will depend on exporting technical expertise developed offshore. A 2004 survey of regional firms found that 43% said exports were more than 30% of their turnover. Mr Runcie's next target is a big upgrade of the rail line south.

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Financing pensions

Hidden treasure

Oct 6th 2005
From The Economist print edition

Pension reform might tempt Gordon Brown to levy another stealth tax

AS THE conference season ends, pledges and rhetoric will give way to decisions and action. High on the political agenda is pension reform. Tony Blair told the Labour Party on September 27th that the government will publish its plans in 2006 after getting the recommendations of the Pensions Commission at the end of this year.

Simplifying Britain's notoriously complex pension system is common ground. The state itself provides a confusing set of tax-financed benefits. Two are based on national insurance (NI) contributions, paid by employers and workers. Employees build up not just flat-rate rights to the basic pension but also earnings-linked rights to the state second pension (S2P). Many are also likely to become eligible for the pension credit, a means-tested top-up.

Many reformers yearn to replace this muddle with one state pension. The National Association of Pension Funds (NAPF) and the Institute of Directors (IOD) recently published proposals for a single pension. Both said that such a reform would eliminate another complexity that is virtually unique to Britain's pension system: contracting out.

At present, employees and their pension schemes can contract out of the state second pension. This essentially means that workers give up their S2P benefits in return for rebates on their NI contributions. The money is invested to build up private pension rights that should broadly match those they have relinquished.

A reform creating a single state pension would sweep away not only S2P but also contracting out. The impact would be substantial. On the latest available figures, 56% of eligible employees were contracted out of S2P. The cost of the rebates to the Treasury, excluding those to public-service unfunded schemes, is £8 billion a year, according to the Pensions Policy Institute.

That sum, worth 1.7% of tax revenues, would go a long way to getting the chancellor out of fiscal trouble. The International Monetary Fund says that “fiscal consolidation”—IMFese for tax increases—is needed if the government is to meet over the next economic cycle its “golden rule” of borrowing only to invest. Analysts think this will require tax hikes of about £10 billion.

In the long term, abolishing contracting out does not alter the public finances one way or another. The government gets its rebates back, which raises current tax revenues. But this is offset by the commitment to pay more in S2P pensions in the future. Since the rebates were set by government actuaries to meet the pension liability that would now shift back to the state, nothing has changed.

In the short-term, however, the abolition of contracting out would help Mr Brown meet his fiscal rules. The rise in tax revenues would help him stick to the golden rule whereas the future rise in public pension spending would not be scored against it. And unlike government debt to bondholders, state pension liabilities do not feature in the Treasury's other rule to keep debt at a

sustainable level.

The pension reforms proposed by the NAPF and IOD call for the government to use the revenue from ending contracting out to boost state pensions now. But Mr Brown might prefer to get rid of contracting out while retaining the current structure of pensions. After all, the chancellor has championed the pension credit as a cost-effective way of targeting pensioner poverty. Furthermore, the pensions industry has been saying for some time that the rebates no longer offer fair value, which strengthens the case for ending contracting out as a reform in its own right.

Abolition would entail some risks. It would reduce pre-funding in the pension system, points out John Hawksworth of PWC, an accountancy firm. Employers sponsoring pension schemes would also need to lower their benefits in order to offset the loss of the rebates. The change would be disruptive, says Raj Mody of Hewitt, a human-resources consultancy; in reviewing benefits, employers might decide to make additional cuts, and even if the overall changes were cost-neutral some employees might end up worse off.

But the reform has the singular political attraction that it deals with what John Ralfe, a pensions analyst, calls “the most obscure aspect of pensions, one that makes people's eyes glaze over”. Much the same could have been said about the dividend tax credits for pension funds that Mr Brown abolished in his first and most spectacular stealth tax eight years ago. Since that first budget in 1997, he appears to have retained his taste for stealth taxation. Insurers complained this week about a £1 billion (the Treasury disputes the figure) bill from some new impenetrably complicated tax measures. Compared with the pain of raising more visible taxes, the abolition of contracting out could prove seductive for a chancellor in a fiscal fix.

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Economist.com WORLD EUROPE

Climate change

Regulate us, please

Oct 6th 2005
From The Economist print edition

The difficulties of a policy on climate change

IT IS not often that businesses clamour for more government regulation. But that was exactly what happened this week when a group of bosses met ministers to discuss climate change.

Many big companies say that they are keen to do their bit to fight global warming. In the absence of clear guidance from the government, though, they are shy of making the first move, since firms that go green will merely burden themselves with higher costs than their less virtuous competitors. With big reviews of both energy and environmental policy under way, they want the government to come up with something firmer than its existing targets on carbon emissions, which are not legally binding. Other rules have been proposed, too: in July Friends of the Earth, a green group, and a collection of power companies, suggested tax incentives for green firms and changes to building codes so as to promote energy efficiency.

All that sounds fine in theory, but coming up with a rigorous and clear policy on climate change will be tricky. Companies are far from unanimous in their desire for new rules. Big firms, so often painted as the villains in debates about the environment, are much keener on the idea than smaller companies. Large firms are often better at planning than small ones, and long-term strategy works best in a stable marketplace. Big firms with dedicated legal departments can absorb the costs of regulation more easily than tiny ones.

Others worry about international competitiveness. Green campaigners would like Britain to set an example to the rest of the world. The Confederation of British Industry, a lobby group, says that passing severe carbon laws without persuading America and continental Europe to follow suit would undermine companies' ability to compete.

The most fundamental difficulty is science. Virtually all scientists believe that global warming is at least partly man-made, but there is much less consensus about the size of the problem. The computer models used by the Intergovernmental Panel on Climate Change, the UN body charged with studying global warming, predict an average world-wide temperature increase of between 1.4 and 5.8 degrees by 2100. With such uncertainty, predictable, long-term policy-making is tricky. In the absence of incontrovertible scientific data, it will be hard to minimise the influence of lobbying and special pleading—from either side of the argument.

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Nuclear power

Going critical

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If Britain wants more nuclear power, it must take some difficult decisions

AFTER years in the wilderness, nuclear power is back on the agenda. Officials have been hinting at a revival for several years, pointing out that it is a carbon-free source of electricity that can contribute to energy security. At first, Tony Blair promised a decision by the end of this parliament. Last week Malcolm Wicks, the energy minister, firmed up the timetable, promising to decide one way or the other by the end of next year. Many observers now believe that ministers will approve new power plants. If they do, they will have to make some tricky decisions first.

Such as about the finances of nuclear power. Historically, atomic energy has been a money pit. Only two years ago the government completed a multi-billion pound bail-out of British Energy, which operates Britain's newest reactors. The pro-nuclear lobby argues that consolidation in energy markets and simpler, cheaper reactor designs have driven costs down in recent years. And experience from South Korea and China, both of which have big nuclear programmes, supports the idea that building several reactors of the same design can save money.

Even so, few observers think that nuclear power pays its way in today's electricity market. Boosters say that schemes like the European Emissions Trading Scheme (ETS), which puts a price on carbon emissions, will in future make nuclear energy profitable.

Some disagree. Robin Smale of Oxera, a consultancy, thinks that more money will be needed. “The problem with the ETS is that member states set the emissions limits, which means they can control the price,” he says. Investors will want stability, just as other businesses do (see article). “If you want a project with a long lifetime and big financing requirements you need something that looks more like a contract and less like a trading scheme full of political risks,” he says.

He believes that the government will have to consider guaranteeing a carbon price. Some might see this as akin to direct subsidies for nuclear power, something that Mr Wicks has ruled out. But Mr Smale points out that renewables generators, which are already subsidised, would benefit from the new scheme as well.

Keith Parker, chief executive of the Nuclear Industry Association (NIA), says planning needs reform. Sizewell B, the last nuclear power station commissioned in Britain, needed 14 years and one of the most expensive public inquiries in British history before it was ready. He says that new planning policies are needed to prevent a repeat performance and calm investors' nerves. Planning applications for big renewables projects are already handled by Whitehall rather than by local authorities, and some observers think something similar may be needed for nuclear power. Mr Parker wants changes to the licensing regime, so that once a reactor type is approved, inquiries into safety design do not have to be revisited each time one is built.

Decommissioning costs may be a sticking point. Earlier in the year the government launched the Nuclear Decommissioning Authority, a public body that will dismantle Britain's state-owned nuclear sites at a cost to taxpayers of £56 billion. If taxpayers want to avoid a clean-up bill, they need a

way to finance future clean-up costs privately. They could follow the American approach, in which nuclear generators are required to set clean-up money aside. But forecasting costs decades into the future is as much luck as it is judgement. If anything goes wrong, taxpayers will have to pay.

A policy on nuclear waste is overdue. Britain has been splitting atoms for half a century and governments have been skirting the issue of waste disposal all the while. The problem is not technical (every expert recommends burying the waste deep underground) but the difficulty of finding someone willing to accept it. Experience from Finland, which finalised its waste-disposal plans in 2001, suggests that towns with ties to the nuclear industry are the most tolerant, though strong opposition is likely wherever the stuff ends up. Again, investors want a clear plan.

All of this feeds into the most important challenge of all: persuading voters that nuclear power is a good idea. This may not be as difficult as you might think. A poll conducted in January for BNFL, a state-owned operator, showed that more people had a favourable impression of the nuclear industry (28%) than an unfavourable one (26%) for the first time since 1999. It may be harder for the government to convince its own MPs: a MORI poll last week showed 45% of Labour MPs opposing new nuclear plants, with only 36% in favour.

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Bagehot

David Davis has a fight on his hands

Oct 6th 2005
From The Economist print edition

He is still the front-runner to be his party's next leader, but in Blackpool David Davis was not the best candidate

Get article background

WHAT a good idea it turned out to be. The not-quite-gone, but almost-completely-forgotten Michael Howard's derided plan to hold a party conference without a party leader has given the Tories their best week for years. A conference that many expected would be a morbidly introspective affair as the party attempted to come to terms with the reasons for a third shattering electoral defeat was nothing of the kind. Instead, there was excitement, optimism and even some tentative signs that Tories are at last trying to understand what they must do to win back power.

But do not get carried away. A leadership contest is inherently thrilling (at least for the kind of people who enjoy going to party conferences). Each adrenaline-pumped contender has had to perform, to persuade and to make “the speech of his life”. Rival gangs of backers roamed the bars, bending ears, grabbing elbows and, when absolutely necessary, buying drinks. There is a feeling of being caught up in something important. At this heady moment, everything seems possible, each candidate a projection of his supporter's dearest hopes.

But on December 5th, when the votes of some 250,000 party members will be in, a more prosaic reality will reassert itself. There will be a real leader with real flaws, who, thanks to an unsatisfactory electoral system, is unlikely to be the first choice, either of a majority of MPs or of the party's activists. Ahead of him will be the grind of four more years in opposition and the task of rebuilding a party that, for all the buzz in Blackpool this week, has not even begun to convince the country that it has changed.

That task will be none the easier if, as still seems likely, it falls to David Davis. Although Mr Davis

was comprehensively outplayed this week by both Ken Clarke and David Cameron, the leadership is still his to lose. Thanks to a disciplined campaign at Westminster run by some of the party's most fearsome former whips, Mr Davis has so far rounded up endorsements from at least 66 of the party's 198 MPs. If they vote as promised, Mr Davis needs just one more to guarantee that he will be one of the two candidates going forward to the ballot of party members.

By the final round of voting at Westminster, Mr Davis is banking on his team winning almost twice as much support as his nearest rival. If it secures such a lead, the Davis camp will leave the party's activists in no doubt that it would be a dreadful mistake to impose as leader on the MPs anyone other than their man. Deference is not what it was in the Tory party, but the members are likely to take such a warning seriously—after all, however unfairly, they got the blame in 2001 for choosing the disastrous Iain Duncan Smith.

Whether the Davis battleplan survives the excitement of Blackpool is another matter. Mr Clarke electrified the conference with a typically bullish and brutal critique of the government's failings. Mr Cameron provided hope and uplift in a speech that combined passion with precocious professionalism. By contrast, when Mr Davis had his turn, he seemed to know neither how to attack nor how to inspire. He was dull and flat. Even the almost comically ideological Liam Fox beat him for rhetoric and vision.

Mr Davis's supporters explained that big set-piece conference speeches are not their man's strength. But his performance at fringe gatherings was not much better. On policy, he was routinely slipshod, suggesting that such countries as Switzerland, the Netherlands and Sweden had better public services than Britain despite being poorer, when, over a 20 year period they have been richer according to the relevant measure of GDP per head and have spent heavily on schools and health. He also made the extraordinary assertion that a restrictive immigration policy would help downtrodden illegal immigrants, such as the Morecambe Bay cockle-pickers. In fact, the more difficult legal immigration is made, the more the illegal sort will flourish. And his political instincts let him down, too. Honesty is a virtue, but his macho claim that, while he might once have changed a nappy in an emergency, he had never cooked a meal at home was a strange boast for someone wanting to lead a party that has haemorrhaged support among women and younger voters.

Mr Davis has his strengths. He is tough, ambitious and more strategic than any of his recent predecessors. He also has an easy, jocular confidence. He commands fierce loyalty. But the question many people in Blackpool were asking was whether choosing an old-fashioned machine politician as leader was really the best the party could do.

A run for his money

For all the growing misgivings about Mr Davis, if Mr Clarke is his opponent in the ballot of party members, he should scrape through. Mr Clarke is a splendid old war-horse, but he remains a divisive figure for many Tories, who cannot bring themselves to forgive him for his pro-European heresies.

But if the choice is Mr Cameron, a different and fascinating situation could develop. In the past week Mr Cameron has acquired that most precious political asset—momentum. Where Mr Davis has under-performed, he has out-performed. A large focus group assembled by “Newsnight”, a current-affairs programme, which was given information about each of the candidates, swung heavily behind Mr Cameron. The more they saw of him, the more they liked him. The same seemed to apply to the activists in Blackpool, now returning to their constituencies. If the newspapers and television decide that Mr Cameron is the coming man, Mr Davis could face a stiffer fight than seemed possible only a few days ago, especially if Mr Clarke's support transfers

to the Cameron camp before the final round of voting.

Mr Cameron is still a punt. He has grit and resilience, but he is young and untried. He has the disadvantage of not yet being politically fully formed. Mr Davis's disadvantage is that he is.

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The sun also rises

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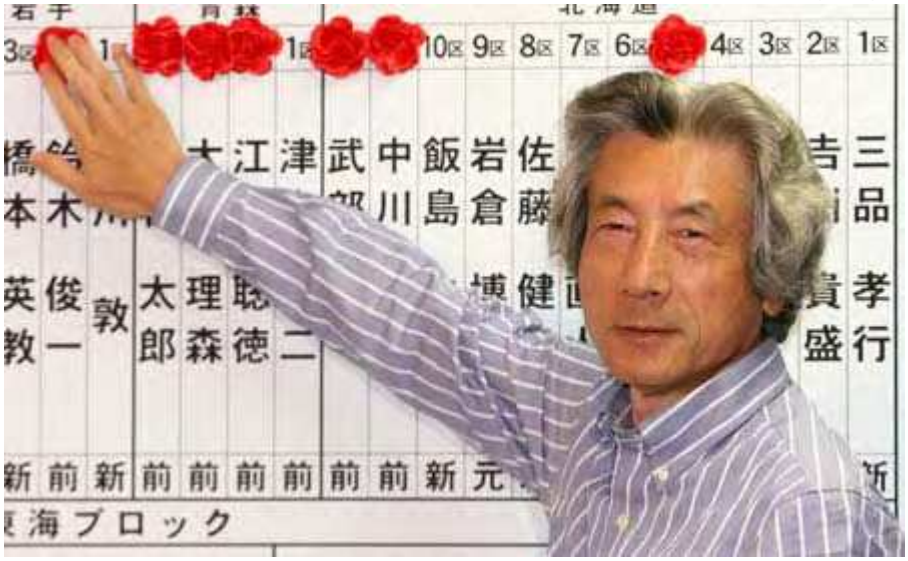
From The Economist print edition

Getty Images



Japan is at last ready to surprise the world by how well it does, not how badly, writes Bill Emmott, editor of The Economist

Get article background

NO COUNTRY in modern history has moved so swiftly from worldwide adulation to dismissal or even contempt as did Japan, in a process that began more or less as the temple bells were tolling in the new year of 1990. In the 15 years that followed, amid crashing stock- and property markets, mountains of dud debt, scores of corruption scandals, vast government deficits and stagnant economic growth, Japan mutated from being a giver of lessons to a recipient of lectures, all of which offered recipes for its reform and revival. Those lectures, although received politely by a newly self-deprecatory Japanese elite, seemed to be ignored. Now, however, the time for lectures is over. Japan is back. It is being reformed. It is reviving.

Really? The very unJapanese event that took place on September 11th—a snap general election called on a policy issue and won in spectacular fashion by the reformist prime minister, Junichiro Koizumi—has changed perceptions of Japan as an irredeemable dud, but not much. After all, the case for cynicism is compelling.

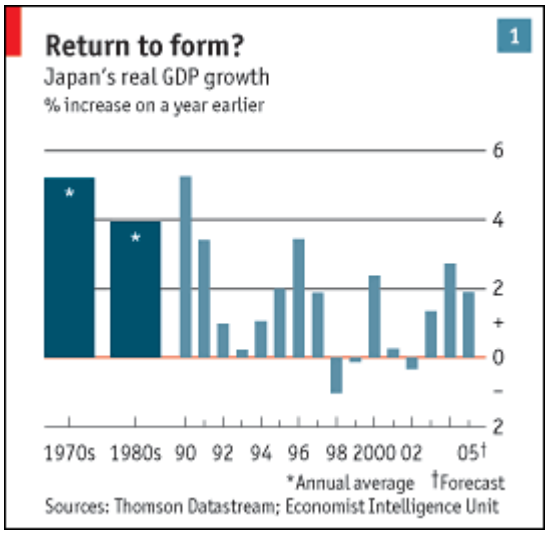
There have been several false dawns during those 15 dismal years, most notably in 1996-98 when an incipient recovery turned into a fresh recession and produced both a banking crisis and an apparent enthusiasm for reform. Since then, Japan has suffered a price deflation that has still not come to an end. Since 2001 it has had a prime minister, that same Mr Koizumi, who has talked a lot about reform but whose real achievements remain rather hard to get your arms around. Moreover, the OECD recently rated Japan's potential rate of GDP growth for the rest of this decade at a mere 1.3% a year, on the basis of poor productivity growth and a population that is shrinking and ageing. Politics didn't even come into it.

But remember. During the 1980s, when adulation (or fear) of Japan was at its peak, many observers made the mistake of assuming that because some things in the country plainly worked extremely well, everything did, so everything must be worth emulating and the trend must be ever upwards. That is why your present author named a book he published in 1989 “The Sun Also Sets”. Japan's sun does not only rise, the book argued; trends can also bring about their own downfall. Since 1990, the opposite mistake has been made: just because some things have gone badly wrong, so everything has been assumed to be wrong, in perpetuity or at least pending a revolution. Hence the somewhat self-indulgent title of this survey: the Japanese sun does not only set, either. It also rises, and looks likely to do so from now on.

For the case for greater optimism is also strong. It is not based on any notion that Mr Koizumi's victory represents the start of radical change. Nor is it intended to suggest that privatisation of the postal savings system—the reform issue around which September's election was fought—will somehow magically turn Japan from a sloth economy to a growth one, for it won't. Rather, it is based on the view that Mr Koizumi's victory is the culmination of a long period of incremental change, bringing welcome confirmation that that change is not likely to be reversed.

Even after his landslide win, it is not inevitable that Mr Koizumi will get his way, for his party's rules stipulate that he will have merely a year as leader to exploit his new mandate. Still, there is a chance that the party will extend his term, but also a likelihood that any successor will follow the Koizumi script. This would mean that the size and role of the Japanese state will shrink, in a slow but remorseless process over the next decade or so. That will gradually help improve the public finances, which are in a mess; gradually help reduce the financial distortions that have arisen from the state's role in banking; and gradually help reform politics, which had become dependent on state cash and power.

Gradually: that could be Japan's watchword. The country has not had a revolution, nor has it gone through the “shock therapy” of reform that Margaret Thatcher deployed in Britain in the 1980s or that some central European countries tried in the 1990s, and it is not likely to go through that now. For this is not a country of revolutions, but rather one that tends to follow a course faithfully and steadily once it has been agreed upon and set.



For the past decade, although the main approach to the country's immediate macroeconomic and financial woes has been one of muddling through and hoping for the best, there has been a gradual process of reform, of setting new courses and parameters for behaviour. This has consisted of an accumulation of many small changes—some in politics, but also in financial regulation, in corporate law, in public opinion, in capital markets, in corporate mores. The two big questions have been, first, whether that process will endure; and, second, whether the burdens of the past—debt, deflation, corruption, labour protection—will continue to overwhelm the benefits that come from those changes, or whether Japan might soon be in a position to grow and develop again as a normal country might.

September's election answered the first question. But to answer that second question, it is no good speculating about politics, nor expecting the politicians to produce radical, invigorating reforms. They have neither the power nor the capability for that. The place to look is not in the fancy headlines of politics but deep in the fabric of Japan's economy and society. And although there may not be one single reason to expect a transformation, there may well be one single field of data that currently holds the clue as to whether economic recovery is going to be sustainable in

the longer term, as well as exemplifying some of the biggest changes that have taken place. That field is employment and wages.

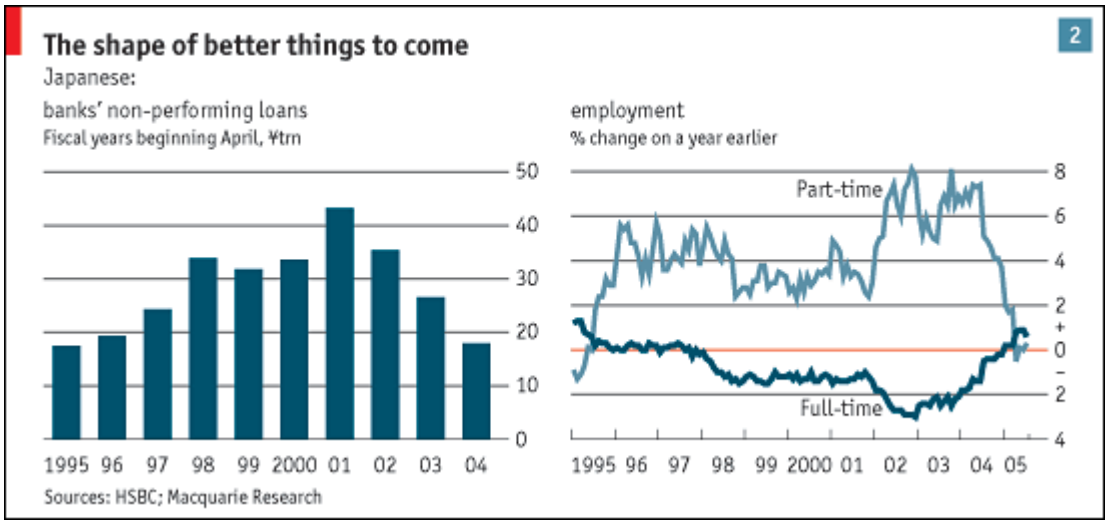
Lessons from the labour market

The Japan of old was known as the country of “lifetime employment”, a somewhat exaggerated but still important notion that in return for loyalty and flexibility big employers typically offered a lifetime commitment to their workers, with associated company unions, generous fringe benefits and pay rising according to age and seniority. That also made for a fairly egalitarian society. Shock therapy would have shattered the lifetime notion, producing a big rise in unemployment. So it never happened: most big companies chose to maintain their commitment, asking workers to take pay cuts and waive bonuses rather than lose their jobs, but ceased to hire new graduates. Less than half as many new graduates were hired in 2003 as in 1997.

But also, helped by changes to employment law, firms found flexibility in another way: by hiring part-timers and others on temporary contracts, both at far lower cost than for regular workers. In 1990 such “non-regular” workers made up 18.8% of the labour force. Earlier this year, that figure reached 30%, which in Japan's 65m-strong labour force means roughly 20m people. Those workers are predominantly women, the young and the fairly low-skilled. Since 2003, the law has allowed contracts to be counted as temporary, and thus cheap, for up to three years. The use of contract workers remains forbidden in some sectors that employ lots of people, including health care and construction, but has gradually become permitted almost everywhere else. Canon, for example, a successful electronics firm that still firmly maintains a lifetime commitment for its “core” workers, employs fully 70% of its Japanese factory staff on such “non-regular” terms, up from 50% five years ago and 10% a decade ago, according to Fujio Mitarai, Canon's president.

This new labour flexibility has contributed to a boom in company profits and to the paying down of debt. In 1998 workers' pay equalled about 73% of corporate earnings. By 2004 the proportion had dropped to 64%. Other factors helped too, most notably a big rise in exports to China in 2002-04, which revitalised manufacturers of all kinds, whether metal-bashers or precision engineers, and a series of bank nationalisations and mergers in 1998-2004 during which bad loans worth trillions of yen came good or were written off.

As a result, the gigantic pile of dud corporate debt for which Japan became notorious in the late 1990s is now a lot smaller: from a peak of more than ¥43 trillion in 2001, non-performing loans held by banks have more than halved to less than ¥20 trillion (see chart 2). The number is now also thought to be more or less accurate, whereas until 2001 or so official figures for non-performing loans were appallingly and deliberately underestimated.



Labour flexibility came at a price, however. Falling wages boosted profits but also weakened demand. In recent years, consumption has been sustained only by households choosing to save less of their incomes: the Japan that in the 1980s was reputed to be a nation of savers now has a household saving rate of merely 5% of disposable income, one-third of its level in 1990. New jobs have been created, but as 2005 began most were still part-time or on temporary contracts. Part-time workers in Japan get on average less than half the full-time hourly wage. The lowlier contract workers, such as shelf-stackers in convenience stores, can expect ¥600-800 per hour, which is well below the British legal minimum wage. Little wonder that an economic commentator, Takuro Morinaga, topped the bestseller charts in 2003-04 with a book on how to live on ¥3m a year. So much for the idea of Japan as a high-cost country.

As long as wages were falling and the new employment being created was the cheaper, less secure sort, there was little chance that economic growth could become truly sustainable. The cost-reduction and flexibility may have been a necessary condition of eventual recovery, but could not itself bring it about. Rather as in America during the Great Depression, declining demand has helped to neutralise improvements taking place elsewhere in the economy. Moreover, there are limits to what export-led growth, the great hope of 2002-04, can achieve, given Japan's already large current-account surplus (3.6% of GDP), the chance that the yen will strengthen against the dollar and the danger of slower demand in Japan's top foreign markets, China and America.

Since April, however, the employment data have shown something new and more promising: full-time employment is growing faster than the part-time sort for the first time in a decade, and although some of that growth is still in full-time contract work, regular employment is rising too. Wages are also rising, at their fastest rate since 1998 (which mainly means they are simply rising, at last), and bonuses are again being paid.

It is still early days—too early to tell how strong this rise in employment and incomes will prove to be. Probably, its effect will be gradual: people may try to rebuild their savings rather than spending all their gains, competition from low-cost China and India will help limit wage gains, and firms scarred by the past 15 years are unlikely to embark upon an investment and hiring binge. What this development does suggest, though, is that the last of the three excesses that have burdened the economy since 1990—excess corporate debt, excess capacity and excess labour—may now finally be on the point of elimination.

Magnum

Learning to spend again

Elimination is probably too strong a word, for whether something is excessive is a subjective question. The ratio of debt to operating profits for large and medium-sized firms is down to levels typical in the 1980s, ie, less than 10%, compared with 15-20% at the peak in 1999. Smaller firms still hold debt of nearly 15% of operating profits, but that too is down from over 20% in 1999. Excess capacity is a particularly subjective matter: the capacity-utilisation rate reported by the Ministry of Economy, Trade and Industry is back up to 1992 levels, and businessmen's perceptions, as reported in the Bank of Japan's regular Tankan survey, are that excess capacity has largely disappeared.

The important issues now, though, revolve around risk, stability and incentives. During the 1990s, although Japan experienced only stagnation rather than collapse, there was always a risk that collapse might come. With corporate debt cleaned up and banks reformed, that risk has gone. Banks certainly think so: their lending has recently started to expand again for the first time since 1998. The alternative now seems to be either slow growth or faster growth, not growth or slump. Moreover, an economy that relies on increases in private spending, by households and by companies, is likely to follow a more stable path than one that depends solely on export demand or public spending. What matters most, though, is how that spending will be used. And that is a question of whether the incentives governing such spending have changed: the incentives for companies to waste the money or use it well, and the incentives for politicians and bureaucrats to abuse it, steal it or otherwise distort it.

A very stealthy revolution

That is where the many other small changes come in. A simple way to understand what happened to Japan in the 1980s and 1990s is that a country with many strengths, especially a high average level of education, formidable technology and powerful social co-ordination within companies, came to lose its basic disciplines and incentives, particularly in the late 1980s when it experienced one of the biggest asset booms in world history. Flushed with success and with seemingly costless capital, companies expanded and diversified recklessly. Banks lent regardless of risk or business viability. Bureaucrats and politicians resisted calls for deregulation that could have extended competition and encouraged innovation, because they did not think it was necessary. Interest groups anyway blocked change, chiefly by bribing politicians. The mass media were largely suborned by the political and corporate establishment.

The collapse of the stock- and property booms after 1990 and the ensuing recession might have been expected to shake all this up. It didn't, for two main reasons. The first was that the principal economic response to the slump, ie, massive public-works spending, further enriched some pressure groups and many politicians, making them even more able to resist change, and an expansionary monetary policy deadened the price mechanism that ought to have imposed discipline. The second was that for a mixture of social and psychological reasons, neither bureaucrats nor companies chose to admit what was really happening.

A 15-year gradual work-off of the excesses inherited from the 1980s would not have been what most analysts would have recommended or even expected in 1990, whether they were rude foreign lecturers or polite Japanese. And it has been a more painful period than any visits limited to prosperous Tokyo would suggest. Provincial cities and rural areas have suffered greatly, with shuttered-up streets and rising levels of poverty. Suicides have soared, up more than 50% since 1990 to 34,500 in 2003. By Japan's standards, crime has risen too, though it remains low in comparison with America and most of western Europe. Still, compared with what might have happened in most other developed countries had they gone through the same prolonged experience, Japanese society has remained remarkably stable.

Provincial cities and rural areas have suffered greatly, with shuttered-up streets and rising levels of poverty

Yet although society has been stable, the appearance of policy paralysis is misleading. Actually, bit by bit, step by step, a great deal has been changed, in what may come to look with hindsight like a sort of revolution by stealth. The changes are still continuing and being battled over, so it is too soon to judge whether that word will in the end be justified. But what this revolution-in-progress has already done is to alter many of the incentives surrounding political and corporate behaviour.

It needed to, because in 1985-95 Japanese companies proved incredibly bad at using their own money—or rather, their shareholders' money. Neither commercial law nor the courts helped the shareholders' cause very much. Banks supposedly provided the discipline in the system through their ability to intervene in their big customers' affairs when things went wrong, but such interventions became rarer as the asset bubble inflated, and then rarer still once the banks got into at least as much trouble as their customers. Then, banks kept alive what became known as “zombie” companies for fear of acknowledging their bad loans, of creating unemployment or of upsetting the whole collective applecart.

This used to be called financial socialism, which was meant as a compliment. That time has long gone. Now, a joke is circulating in Tokyo about Chinese students on a course there. Someone asks them why they spend so much time with other Chinese rather than with Japanese students. Their answer: because we are afraid the Japanese might teach us communism. The way things are going, the joke might soon become obsolete.

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Capitalism with Japanese characteristics

Oct 6th 2005
From The Economist print edition

Suddenly, shareholders are beginning to matter

Rex Features

Mr Horie is a livewire too

TAKAFUMI HORIE is proof of the rewards of failure—and of “Livin' on the edge”, which is what he called his company until he bought an internet portal called livedoor and adopted its name. This 32-year-old's daring takeover bid earlier this year for the venerable media group Fujisankei Communications, via its radio subsidiary Nippon Broadcasting System, ended in defeat: Fuji found a white knight to hold a blocking slab of its shares and forced Mr Horie to retreat with only a small profit and a modest business deal between Fuji and livedoor. In July 2004 his bid for a baseball team, the Osaka Kintetsu Buffaloes, also failed. Yet the attendant publicity helped livedoor hugely: page views at its portal in June this year were more than six times higher than a year earlier, and the company has raised its advertising rates twice in less than six months. It remains a distant third in the internet portal business behind Yahoo! Japan and Rakuten, but its share price has stayed high despite stock dilution and the Fuji bid's failure, and its earnings multiple is higher than that of Yahoo! Japan.

“The nail that sticks up”, runs a hoary Japanese saying, “gets hammered down.” Yet Mr Horie is an upstanding nail who has become famous as well as much admired, according to opinion polls, for his willingness to challenge old ways of doing things. He even ran (unsuccessfully) for the Diet in September's elections. And he is not alone in breaking taboos. Hot on the heels of his bid, in July a young construction design firm, Yumeshin Holdings, launched a hostile tender offer for an older firm, Japan Engineering Consultants. And last year Sumitomo-Mitsui Financial Group, one of Japan's biggest banks, barged its way into a friendly merger deal between two other mega-banks, Mitsubishi-Tokyo Financial Group (MTFG) and UFJ Holdings, offering to buy UFJ for a specified price. That may sound mundane, but to Japanese sensibilities it was shocking, because UFJ's board had already accepted the merger proposal, even though no price had been set.

A related bank, Sumitomo Trust, weighed in too, seeking a court injunction to block the MTFG-UFJ merger on the ground that it violated a prior deal under which it was to buy a UFJ division. In the end, after a protracted battle in the courts and the capital markets, MTFG prevailed, but only at a

cost: cash compensation for Sumitomo Trust, a big cash injection into UFJ to help it deal with its bad loans and a higher price for shareholders than it would otherwise have been paying.

The livedoor-Fuji battle, the Yumeshin bid and the mega-bank sumo-wrestling match illustrate three important developments. The first is a new willingness to use the courts as arbiters in corporate disputes, which reflects both changes in attitudes and changes in the law. Livedoor managed to get several of Fuji's attempted defence manoeuvres struck down by the courts before Fuji's white knight came along. Yumeshin failed to block Japan Engineering's defences of a stock split and an equity warrant issue, but the Tokyo District Court laid down reassuring criteria for their use: that they must not simply be in the board's self-interest, and that they are subject to shareholders' approval.

Secondly, a change in the ownership pattern of publicly traded shares is making transactions and challenges easier. In 1992, according to the Ministry of Economy, Trade and Industry, 46% of all listed equities were held as cross-shareholdings by related companies, and only 6% by foreign investors. In 2004, cross-shareholdings accounted for merely 24% of shares whereas foreign ownership had risen to 22% of the total. However, that foreign slice is volatile, moving up and down along with investing institutions' perception of the Japanese market. Cross-shareholdings first became prominent during a fright about hostile takeovers in the 1960s, so there is a chance that scared managements may now seek to rebuild them. Against that, though, new capital-adequacy rules due to take effect in 2006-07 will force Japanese banks to sell more of their holdings.

The third development is still small but is emerging steadily. It is the arrival on the scene of funds and partnerships willing to use their investments to challenge existing managements or to act as intermediaries to facilitate mergers and disposals. One example is M&A Consulting, a shareholder-activist fund that also profited from building a stake in Nippon Broadcasting System earlier this year, and which has specialised in pressing managements to use their cash piles to raise dividends and make share buybacks. Another is Privee Zurich Turnaround Group, a private-equity fund which despite its name is thoroughly Japanese, and which has also flirted with hostile bids. A third is Advantage Partners, a private-equity investor chiefly in the business of acquiring assets from companies being split up or turned around.

Alongside these new Japanese species there are the larger and more familiar foreign funds: Ripplewood Holdings, which with J.C. Flowers & Co made a fortune by buying Shinsei Bank, formerly Long-Term Credit Bank of Japan, from the government in 2000 and transforming it; Carlyle Group; Lone Star; Cerberus; and several others. By and large, though, it is the Japanese upstarts that are acting most aggressively, whereas the foreign funds try to stress how socially responsible they are.

Both make up only a small slice of market activity. But no matter: in any business, pressure on the margin can influence the rest. To some degree, indeed, these ginger groups have been encouraged by people in the Japanese establishment with just that thought in mind. Mr Horie may be an outsider, but plenty of the activist funds are run and staffed by well-connected former bureaucrats and by people in their 30s and 40s who lost their jobs or their loyalty during the banking meltdown of the 1990s. M&A Consulting, for example, is run by three partners, two of whom are former bureaucrats and the third used to work for Nomura Securities. An early investor in the firm, and a crucial provider of introductions, was Toshihiko Fukui, before he became governor of the Bank of Japan. Similarly, Ripplewood managed to recruit several senior Japanese to its board, including Minoru Makihara, then chairman of Mitsubishi Corporation, the trading and investment firm that epitomises the Japanese establishment.

The livedoor bid for Fuji illustrated another point about Japanese capitalism: that for a seemingly cosseted, conformist activity, it is strikingly unregulated. When almost everyone obeys unwritten

rules, little attention needs to be paid to the written ones. So the supposedly heroic Mr Horie was able to mount his bid in ways that would be considered outrageous in London or New York: he built up his 35% stake in NBS in off-market trading, diluted his own investors' shareholdings without consulting them and never offered a standard price to all NBS shareholders.

The wild west goes east

Part of the problem is that takeovers and other pressures from shareholders were long considered taboo or irrelevant. The protective role of main banks and cross-shareholdings was enough to regulate matters. Now that both of those protections are weakening, there is a fairly broad consensus that the law and the regulatory system need to be changed. But that change is happening slowly. An optimistic view is that the process is at roughly the halfway stage. Still, some important progress has already been made.

One of the worst corporate sins of the 1980s was the use of subsidiaries to hide problems, park surplus staff or disguise adventures: they did not have to be consolidated into profit-and-loss accounts. New holding-company and accounting laws in 1999-2001 changed that. A so-called “big bang” of financial reform in 1998 was in truth more like a slow drum roll, but it brought in a new regulatory body, the Financial Services Agency, with the job of supervising financial institutions and accounting practices.

One obstacle to firms selling divisions and subsidiaries to each other was a rule that required an appraisal of all the division's assets by a court-appointed inspector. In 2000 a new law abolished that rule for “non-core” business units, defined as small, underperforming ones. That does not go far enough—firms ought to be free to sell what they like—but it has stimulated a lot of trading in distressed assets. Another new rule has reduced the capital requirement for new limited companies to just ¥1, down from ¥3m.

Virtually the whole of the Japanese commercial code is being overhauled along similar lines. Nevertheless, with politicians afraid of instability and especially foreign takeovers, and under pressure from big employers, many of the reforms so far have been as helpful to corporate defence as offence. Laws already passed have permitted companies to offer shares with differential voting rights, to grant stock acquisition rights through options and warrants, and to set up such provisions as a “poison pill” to be deployed in the event of a takeover bid.

On the other hand, the law has defined the proper purposes of such measures as well as the need for shareholder meetings to approve them. And it has made proxy votes against such measures easier. All that has helped boost the role of the courts. Earlier this year the Tokyo District Court rejected a crude poison pill proposed by Nireco, an instrument-maker.

The role of shareholders has been boosted too: at the spate of annual meetings on June 29th shareholders rejected poison-pill proposals at several big firms, including Tokyo Electron, Fanuc and Yokogawa Electric. Many other similar proposals passed, but significantly even some Japanese institutional investors took part in anti-management votes. Previously they had been quiescent.

One provision the Diet (parliament) considered too hot to handle was a reform to allow foreign firms to use their own shares as currency in acquisitions in Japan, whether hostile or friendly. This would bring the rules for foreigners into line with those already in place for Japanese companies. But in April the measure was postponed for a year. Unless there is a big controversial cross-border battle in the meantime, however, it stands a good chance of being passed in due course.

Another area of law that needs further refinement is the definition in corporate governance of outside directors: they have been given an enhanced role, especially in big firms that choose to

adopt an American-style board committee system, but there is no requirement that they be wholly independent. Seibu, a railway and property giant whose autocratic boss, Yoshiaki Tsutsumi, was charged with fraud earlier this year, held no board meetings for seven years. It did have outside directors, but they all had business relationships with Mr Tsutsumi.

For all the fuss over hostile takeovers, however, such battles are rare even in America, which sees barely one each year. Even the theoretical possibility of such an event, though, helps put pressure on managements to improve their profits as well as to pay dividends to shareholders. Japanese corporate profits are at a record high mainly for other reasons, but market pressure has literally paid dividends: in the past seven years the dividend yield for firms listed in Tokyo has almost doubled (see chart 3).

Even so, the most important sort of transaction, in Japan as in America, is the friendly sort, whether involving whole firms or divisions of them. In the first eight months of this year, according to the *Nihon Keizai* financial daily, 1,735 M&A deals were completed, 28% up on a year earlier.

As James Abegglen, a veteran consultant and scholar in Tokyo, observes in his recent book, “Redesigning the Kaisha”, the consolidation of whole industries during the past decade has been impressive: from 14 oil companies to four; from seven big cement firms to three; from 14 pulp and paper companies to three; from seven industrial gas firms to three; from five big steel firms to four; from 15 big banks to just three. And big companies have traded or closed thousands of subsidiaries.

More competition, please

Neither the lawyers nor the financial advisers have been idle. Many of Japan's biggest and most internationally famed firms are now more focused and efficient than before. Their scale and new concentration will make it easier for them to compete abroad. But for them, and even more for the huge array of domestic firms, there is another, more important question: is there enough competition at home to keep them all on their toes?

Deregulation during the 1990s, in fields such as telecoms, transport, energy, finance and retailing, benefited consumers to the tune of 4.6% of GDP in 2002, or so the Cabinet Office claims. This certainly helped, though the OECD reports that Japanese electricity and telecoms prices, for example, remain the highest among that organisation's rich-country members. But perhaps the biggest issue now is whether Japanese anti-monopoly laws stand a chance of being enforced.

There is certainly some political will to do so. Amendments to antitrust law passed by the Diet in April and due to come into effect early in 2006 will bring four main changes: an increase in the penalties for breaking the law from 6% of affected sales for most large firms to 10%, with surcharges for repeat offenders; the introduction of a new incentive for cartel members to blow the whistle by offering discounted fines for those who come clean early; new powers for the Fair Trade Commission, Japan's trust-buster, to make raids and seize documents; and new powers for the FTC to issue cease-and-desist orders before holding a hearing rather than waiting until afterwards.

That all sounds robust, and the new law was passed despite opposition to its first draft from big businesses. Yet those penalties remain lower than those used in the European Union and America. And in the past Japan has been none too assiduous in enforcing what legislation it had in this area. The OECD notes that there have been only 13 criminal antitrust cases in Japan since 1950, and that no one has ever gone to jail for breaking competition law.

Until 2002 the FTC was a small body with a low status, firmly under a ministry's thumb. However, one of the less noticed moves of the prime minister, Mr Koizumi, was that he shifted the FTC so that it now reports directly to the Cabinet Office, and gave it a new boss and a bit more money. Whereas in 1995 the FTC had 220 investigators and a budget of ¥5.24 billion, last year it had 331 investigators and a budget of ¥7.82 billion.

There are some omens that bode well for stronger enforcement. Just as the courts have played a bigger role in securities disputes, so the Tokyo Stock Exchange acted decisively when Seibu's frauds were disclosed, forcing the firm to delist in December last year. The FTC too has become more active. In March it fined six steel firms a total of ¥6.8 billion for price-fixing. Barely a week goes by without an FTC raid or an indictment of a construction company or a member of staff of the Japan Public Highway Corporation, a soon-to-be-privatised government agency, for rigging bids for bridge contracts. In May, the FTC filed a criminal prosecution of eight such companies.

It could be argued, though, that the TSE acted only once the game was up for Seibu. The bridge scandal too has been convenient for the government: Mr Koizumi wanted to show that privatisation will make a big difference, and to discredit the agency's top bureaucrats sufficiently to ensure that they cannot scupper the plan. Yet if competition enforcement is simply a product of the political winds, what if the winds change?

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New politics, old politicians

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It will never be the same again. Well, not quite, anyway

AFP

One of them stands out

Get article background

IN SEPTEMBER 1998 the cover of *The Economist* carried the headline “Japan's amazing ability to disappoint”, commenting on the government's bungling of yet another bank-rescue plan. It attracted a petulant protest from the Japanese embassy in London. Motoo Shiina, a veteran Diet member, offered a more thoughtful dissent: the correct headline, he said, would have been “The Japanese people's amazing ability not to be disappointed”. Not so snappy, perhaps, but he had a point: surely in no other democracy would the same party that had been running the country continuously since 1955—the Liberal Democrats—have been left in government following a financial crash and an economic slump to which they had found no solution. They did lose power for all of ten months in 1993-94, but then returned to government, albeit leading a series of coalitions. And they have just been returned to power once again in a landslide, giving them their biggest parliamentary majority since 1986, despite having presided over 15 years of stagnation.

That account, of course, leaves out Junichiro Koizumi, who since 2001 has led the LDP and served as prime minister, and whose early slogan was “change the LDP to change Japan”. His electoral genius at first looked as though it might be limited to his photogenic long wavy hair and clever marketing techniques, including his *Lionheart* e-mail magazine. The election result on September 11th, though, proved that there is rather more to him than that. By calling a snap general election over a single issue of economic reform, the privatisation of Japan Post, which had been opposed by rebels in the LDP but also, crucially, by the main opposition party, the Democratic Party of Japan, he managed the seemingly impossible: to cast the LDP, the ultimate guardian of the status quo, as the party of change. No, you might object, he cast himself as the bringer of change, not the LDP. Yes, but under the party's rules Mr Koizumi has only one more year to serve as leader.

Then, unless the rules are changed to extend his term, someone else will inherit the powerful position he has just built for his party. The long-term winner of the September 11th election was the LDP, not Mr Koizumi.

That raises a crucial question: might it all be just a mirage? That thought is raised, first, by how exceptional Mr Koizumi looks when you compare him with other LDP politicians. He has already lasted longer in office than any prime minister since Yasuhiro Nakasone (1982-87), who was himself the longest-serving since the postwar record-holder, Eisaku Sato (1964-72). Although Mr Koizumi has been a career party member and comes from a political family, in politics he is a loner. He is said to have no real party friends and no political support group. Once he is out of power, which could be in September 2006, or at the latest one or two years later, most people expect him to leave politics altogether.

The concern is reinforced if you examine Mr Koizumi's record of pushing his supposedly bold reforms through the Diet in the past four years. To get his way against a lot of opposition from bureaucrats and from inside the party, he broke with tradition by using non-politicians to front his schemes: Naoki Inose, a historical writer, for the privatisation of the Japan Public Highway Corporation, the agency in charge of building roads and bridges that has been at the heart of the country's corrupt and wasteful public-works schemes; Heizo Takenaka, an economics professor and, since 2001, his main economic-reform minister, for the privatisation of Japan Post. Their styles have been very different: while Mr Inose has shot from the lip in the effort to discredit his opponents, Mr Takenaka has beavered away more quietly. But the outcomes have been similar: such reform as has occurred has been heavily watered down. In the case of Japan Post it was even rejected—until Mr Koizumi won his landslide.

No rush

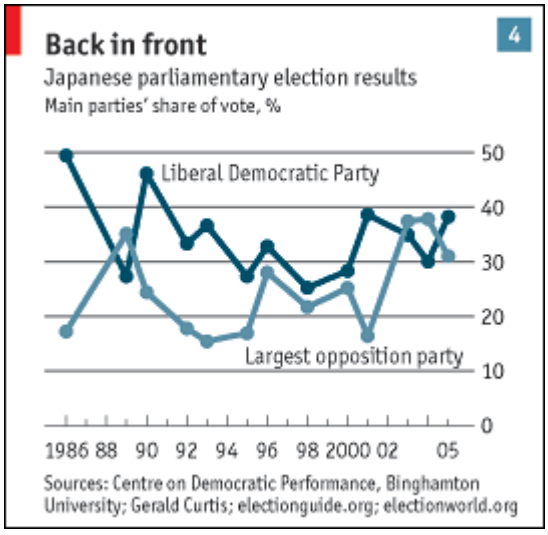
Now, Japan Post will indeed be reorganised and sold off—but over a period of more than a decade. This reform, like that of the highway agency, matters chiefly because the postal savings bank has been responsible for huge distortions in the allocation of funds, and with it a great deal of political corruption. It also matters because, after a decade of high public spending, the national gross public debt has reached 170% of GDP, just when the population is ageing rapidly, opening up the prospect of lower tax revenues and higher medical and pension costs.

Moreover, Japan Post, with subsidised deposits and insurance policies worth ¥330 trillion, taking 30% of all personal deposits and 40% of life insurance, has sat like an elephant in the middle of the financial-services business, skewing the market against the commercial banks and insurers and distorting the price mechanisms that would otherwise direct money flows to the best advantage. So Messrs Koizumi and Takenaka are reorganising the elephant into four separate parts arranged under a joint holding company, handling mail delivery, post offices, savings and insurance respectively. Each will have a profit-and-loss account, but all will remain publicly owned until at least 2017. Savings deposits have already lost their subsidies, though, and the banking and insurance divisions will now have to pay more attention to risk and returns.

Similarly, the highway agency has been split into six, with effect from October 1st, but will remain in public ownership for the time being. The main hope there, too, is that by giving the new roads agencies the obligation to service and repay an accumulated ¥40 trillion of debt, they can be made to act in a more businesslike and disciplined fashion.

The direction of policy under Mr Koizumi is thus clear:

state lending and spending needs to be given new constraints and incentives, he thinks, and ultimately to be shrunk. Later this year, Mr Takenaka says, he will turn his attention to eight other state-owned banks. There was also talk in the LDP's election manifesto of reforms to the public health-care system and to pensions, though few details were given.



Resistance to shrinking the state is stiff, however, not so much on ideological grounds as from interest groups: the construction industry, the bureaucrats, the medical profession, postal workers, all of whom have cultivated politicians to further their cause, particularly in the LDP. That is why Mr Koizumi and his front men from outside politics have struggled to make headway. But it also should prompt reflection on the paradoxical nature of the election result: that Mr Koizumi won his apparent mandate for change against an opposition party, the DPJ, whose manifesto actually proposed much more radical reforms, including a more rapid shrinking of the state. Yet the DPJ was crushed, losing one-third of its seats. Its dull but very worthy leader, Katsuya Okada, resigned.

In the Lionheart's lair

That paradoxical result is testament both to Mr Koizumi's tactical brilliance and to Mr Okada's fatal mistake in getting his party to oppose postal privatisation in the Diet. He did that because the DPJ is an awkward collection, created only in 1996-98, of former LDP members, former socialists and young, genuinely liberal newcomers; the socialists among them retain close ties to the postal workers' union.

For now, though, the DPJ's defeat has destroyed the long-held dream of many political pundits: that Japan would develop a two-party system and have alternating governments. The LDP has regained its traditional dominance. If its coalition with a small Buddhist-backed party, New Komeito, survives, then the pair's two-thirds majority in the Diet's lower house will henceforth allow it to get its way on everything bar a revision to the constitution (which also requires a two-thirds majority in the upper house, where the LDP is weaker, and a simple majority in a national referendum).

But is it the same LDP, or has Mr Koizumi succeeded in changing it, as he promised? Essentially, he has changed it in three ways, none of which is guaranteed to survive his retirement but all of which stand a chance of doing so. The first is that he has severely disabled the system of factions which had long run the party. The factions existed primarily to raise money and to hand out jobs. The introduction of public funding for political parties in 1994 weakened the fund-raising function, as did an electoral reform at the same time that replaced multi-member constituencies (for which party factions therefore competed) with a mixture of single-member seats and proportional representation. Mr Koizumi demonstrated that the factions were weakening by winning the party's leadership election in 2001 against a candidate from the richest and supposedly strongest faction, and rubbed in the lesson by ignoring the factions when appointing his cabinet. They still exist, but for the moment mainly as networking groups rather than power centres.

Mr Koizumi's second change has been to concentrate power in the hands of the party's secretary-general (who is appointed by him) and, within the government, in the prime minister's office. Public funding for political parties had already added to the secretary-general's role, because the money (a total of ¥30 billion a year for all parties) is channelled through each party headquarters.

Since 2003 the same has been true for political funding supplied by Nippon Keidanren, the employers' federation. That stronger party role was on display in August when Mr Koizumi ordered the expulsion of 37 LDP members of the lower house who had opposed his postal privatisation bills.

Under this new regime, advancement within the party depends on loyalty to the leadership more than to the factions. Within the government, too, the leadership has been strengthened. For decades, Japanese prime ministers have been fairly weak figures, with party power diffused by the factions and governmental power dominated by the ministries. That worked, you could argue, because informal co-ordination between the elites in the bureaucracy, the LDP and big business was strong, though that also led to corruption and a lack of accountability. As in other countries, a blend of economic and social change, scandals and public hostility has discredited that old-boy network (which in Japan was called the iron triangle), requiring its partial replacement by more formal, rule-based structures.

Under Mr Koizumi that process of replacement has been accelerated, with more money and staff for the prime minister's office and a reorganisation of ministries to establish a new hierarchy. One main tool of that new control is the Council of Economic and Fiscal Policy, which is chaired by the prime minister and steered by his economics supremo, Mr Takenaka. In theory at least, that council can boss even the finance ministry about.

“In theory” is an important qualification, for much depends on how these new powers are used, and by whom. The third way in which Mr Koizumi has changed politics could determine that, although it is the most uncertain of all. What he seems to have shown is that the way to gain and hold power is by appealing to the public, by making gestures of leadership and by favouring change. Budding successors who would like to continue in that vein, either by choice or because that is the way to win elections, should thus be expected to follow Mr Koizumi's lead in disabling party factions, centralising party power and strengthening the prime minister's office. But will they? A two-thirds majority in the Diet, with an enfeebled opposition, could cause them to move the other way: if you feel untouchable, why bother with public opinion?

Voice of the people, voice of law

By continuing a policy begun in 1998 by an earlier prime minister, Ryutaro Hashimoto, of cutting public-works spending, and now reinforcing it through reforms to Japan Post and the highway agency, Mr Koizumi has probably put an end to pork-barrel politics. The demographic squeeze on public finances will make that almost impossible to reverse. The successors to Mr Koizumi most often mooted within the party—Shinzo Abe, a fairly right-wing former LDP secretary-general who is both youthful and telegenic, and Yasuo Fukuda, a respected former cabinet secretary—suggest that the old stuffed-shirt politics might also be in abeyance. But in a newly victorious party, personal support could shift rapidly. That makes it premature to make assumptions about the succession.

There are, though, more lasting signs that inspire some confidence about the direction and durability of change. The basic incentives surrounding politicians were altered not by the exceptional Mr Koizumi but by those electoral and campaign-finance reforms back in 1994. Political ethics laws from that same period have sought to crack down on corruption, as has a 1994 provision that made candidates legally responsible for illegal actions by their campaign supporters even if they have no direct knowledge of them. These changes have not eliminated corruption by any means, but they have constrained it.

Meanwhile, the voice of public opinion has been getting gently but steadily stronger. Disappointment with the old guard has long been coming through clearly in local elections for city

mayors and prefectural governors, where all sorts of mavericks and outsiders have gained power. September's vote demonstrated at least a desire for change at national level too. Also, though, it has become easier for non-party groups to influence policy outside the Diet. Until 1998, individuals could not readily form lobby groups or associations to promote their particular hobby-horses, because such non-profit organisations had no legal basis. Since then, more than 20,000 have been recognised under a new law. Crucially, they do not yet benefit from the sort of tax exemptions that help explain why America has more than 1.4m non-profits. But even this small vanguard is beginning to have an impact on policy debates, though mainly at local level, and to launch legal challenges to companies and to the government.

That public pressure is now more easily applied thanks to a freedom-of-information law which was passed in 2001, and to quite sweeping judicial reforms that became law in 2002-04. These have resulted in the opening of 68 new professional schools designed to double the number of qualified lawyers over the next decade or so; in the imposition of a two-year time limit on all first-instance trials of criminal and civil cases; in the creation of a new intellectual-property court; and in a new mechanism for involving citizens on judicial panels in criminal cases.

As Jeff Kingston, a professor at Temple University in Tokyo, writes in his excellent book “Japan's Quiet Transformation”, what is happening is that the old system of “rule by law”, with wide administrative discretion and limited legal redress, is being replaced by something more akin to “rule of law”. It is the same trend as that evident in policy co-ordination by elites and the evolution of corporate law: old methods of discretionary power based on unwritten rules are fading away, with new structures and new written rules rising to take their place.

Not surprisingly, not everyone feels comfortable with this increase in the role and number of lawyers. But the increasing role for public opinion is causing some disquiet too. Being popular and campaigning publicly for change, as Mr Koizumi does, is all very fine and democratic, but alongside such virtues has also come a possible vice: anti-Chinese nationalism. Mr Koizumi is no sophisticate in foreign affairs, but in his four years in office he has achieved a steady expansion of Japan's constitutionally limited military role, for example by sending troops to Iraq, and a steady deterioration in Japan's relationship with two of its neighbours, China and South Korea. Until September's election, those worried by such developments could comfort themselves with the hope that the opposition, the DPJ, which adopted a much less assertive, more diplomatic foreign stance, could either become the next government or else restrain the LDP. No longer. Like its old foes in China, Japan is now back to one-party rule.

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New East Asia, old enmities

Oct 6th 2005
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China's growth has changed Japan's region, but is also changing Japan's politics

AP

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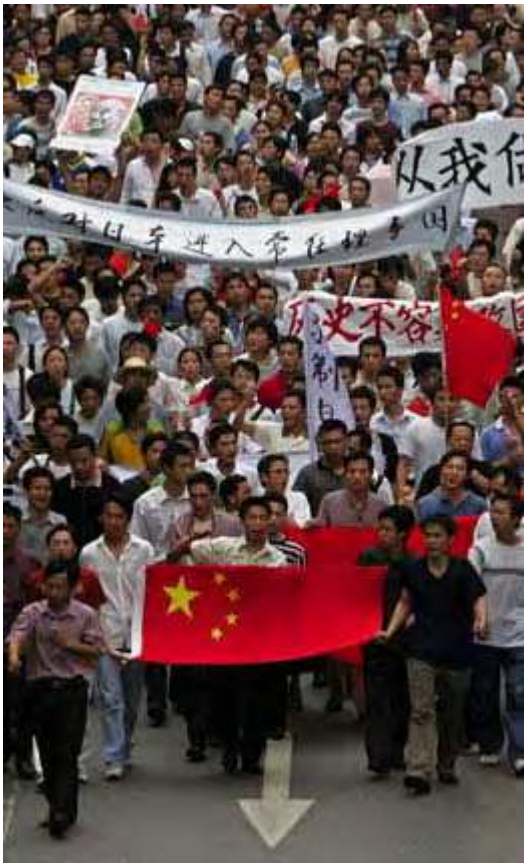

Unfriendly neighbours

AMONG the forces pressing upon Japan, none has changed more since the country's asset-bubble burst in 1990 than its own neighbourhood. Where 15 years ago China was merely a pariah with economic potential, having recently massacred protesters in Tiananmen Square, it now has a better international reputation and a much admired (and two and a half times larger) economy. Where the Soviet Union was then Japan's principal military concern, as it had been for the previous four decades, that threat is no more. Where Japan was then a rarity as an East Asian democracy, with just the young Philippines democracy and the dictatorial sort in Malaysia and Singapore as company, now it has been joined by South Korea, Taiwan, Thailand and Indonesia. Where then Japan depended on exports to America and western Europe, now trade with other Asian countries makes up 45% of the country's total. In both economic and political terms, Japan is no longer alone in Asia.

Yet it is not really together with its new friends either. For one thing has, if anything, got worse: Japan's argument both with itself and, more painfully, with its neighbours about its 20th-century history. This year, there have been mass demonstrations in both communist China and democratic South Korea against Japan, accusing it of refusing to face up to its past. Japan's efforts to gain a permanent seat on the United Nations Security Council if there is a broad reform of council membership have been set back.

Perhaps this doesn't matter much, except to diplomats? Japan has lived with arguments about history ever since 1945, without suffering too much harm. Two factors, however, make that sanguine response look unwise. One is that there is a new threat in the region, or at least a more worrying old threat. That is North Korea, which gave Japan the jitters in 1998 when it tested a long-range missile by sending it flying over Japan; which caused great anguish and anger in 2002 when it admitted at last to having abducted Japanese citizens over several decades; and which now claims to have made several nuclear weapons. Japan is one of the five countries taking part in joint talks with North Korea about these issues (the others are China, Russia, America and South Korea), and stands shoulder to shoulder with its American ally in urging a tough line on the hermit kingdom. But Japan is in a weak position to convince China and South Korea to be tough too, because of its poor relationship with both countries.

The American alliance, first formalised in the US-Japan Security Treaty in 1960 and strengthened

several times since, bolsters Japan's confidence in the face both of North Korea and of those poor neighbourhood relationships. Participation in America's missile-defence plan, while remaining under America's nuclear umbrella, may well be Japan's best form of insurance. Nevertheless, with public opinion sensitised by North Korean provocations, the government has exploited the situation to give itself a bit more autonomy in military and intelligence matters: it has launched its own spy satellites and has been shifting its defence spending away from tanks and towards advanced warships and submarine-detection technology. And in the longer term, North Korean collapse may be as much of a threat as the current regime's sabre-rattling, for unification on the Korean peninsula would create a still-larger neighbour with whom Japan has rocky relations, and might force a rethink about America's military deployments in Asia.

The second anti-sanguinity factor is China. It is not that China poses a big threat to Japan now, in military, political or economic terms. It is expanding its defence spending rapidly, by 12.6% in the past year, but its armed forces remain less advanced than Japan's constitutionally constrained "self-defence forces". The main threat China's defence build-up currently poses is that it might get strong enough to confront Taiwan, which would give Japan an almighty headache. But in that case Japan would not be the only one reaching for the aspirin. In regional politics, moreover, other Asian countries are as suspicious of China as they are of Japan. They may like China's market, but none is dependent on it: in 1999-2004, according to BNP Paribas, South Korea was the Asian country with the strongest trade links to China, but China still accounted for only 10% of its imports and 14% of its exports.

Nor does China represent an immediate economic danger for Japan. The two economies are strikingly complementary, with Japan hogging the sophisticated end of the electronics, engineering and vehicle industries and China occupying the cheaper end. Competition from South Korea for Japan's top companies is much stiffer than that from China: Samsung in electronics, POSCO in steel, Hyundai in cars and ships have all given Japanese firms more pause for thought than have Chinese companies. That, alas, helps to explain why Chinese competition has not yet shocked Japan into economic reform. China is not as big a concern for high-tech Japan as it is, say, for mid-tech Italy.

The real worry is not about present threats at all; it is about a future that appears to be unfolding with disconcerting speed. If China's economy, its regional clout and its defence spending all continue to grow at something like their current rates, then China threatens to overshadow the whole region and, more pertinently, Japan, during the next quarter-century or so. As that happens, other Asian countries might feel forced to swallow their distrust of the Chinese dragon and seek friendship with it for fear of something worse. And China could come to set the rules for regional deals, whether in trade, investment, the environment or even security.

That would injure Japan's national pride but could also hurt its national interests. For Japan, too, would like to be the rule-setter, the top dog in the region. In that regard, what is in prospect is just a resumption of a natural historical rivalry that has lasted a thousand years or more. Like Britain in relation to France and Germany, Japan as an offshore island has always wanted to retain its independence from the continental power. But, also like Britain, it has an interest in gaining influence over trends in its neighbourhood, lest they become harmful to it. That wasn't necessary for 45 years after 1945. Now, the same trends that are making such influence necessary are changing Japanese politics in ways that risk making it harder to attain.

Soft nationalism or hard?

The combination of North Korean provocations and Chinese bullying over history are pushing Japanese politics further to the right. Even the once slavishly pacifist left-wing daily paper, the *Asahi Shimbun*, has adopted a more strident line especially on North Korea but also on China's

recent anti-Japanese demonstrations. And a dispute over the rights to oil and gas in an area of the East China Sea claimed by both countries has provided a test-case of Japan's determination: if Japan gives way to Chinese pressure over the Chunxiao gas field, it is said, then where will China's expansionism end? The dragon is hungry for resources and will always push for more. Lines must be drawn.

The sort of nationalism being exhibited in Japan in response to such disputes is much milder and less worrying than that shown in either China or South Korea. Japanese nationalist fringe groups go around in loudspeaker vans touting their ideas, as they always have, but ordinary Japanese have not matched their neighbours by marching or rioting. And there is no consensus about how best to react: whereas LDP hawks want to deal with territorial disputes by sending drilling ships and risking confrontation, plenty of politicians would still prefer a quieter response.

What seems to be happening, though, is that in response to Chinese pressure Japan's position is hardening. The annual visits made since 2001 by the prime minister to the Yasukuni shrine in Tokyo, long Japan's principal memorial to its war dead, are a case in point. They have made many Japanese uncomfortable, especially businessmen wanting to sell their goods in China. Some debate has taken place about whether alternative memorials might be nurtured or created (see article), or how the history issue might otherwise be defused. But whereas similar Chinese and South Korean protests at official visits to the shrine in the 1980s by Yasuhiro Nakasone, Japan's most recent openly nationalist prime minister, led speedily to a consensus that the visits should be stopped, the protests about the shrine and about the small number of Japanese history textbooks that whitewash the country's war conduct now seem to strike more Japanese as unfair. Japan has apologised for the war on many occasions, runs the argument, but the neighbours will never be satisfied.

This new firmness in Japan's foreign policy, or at least in its opinions about itself and its region, has coincided with a debate among diplomats and politicians about the right approach to East Asia. For many years, Japan has been leery of efforts to establish Asian regional institutions, for equal and opposite reasons: it has feared that its natural leadership of such entities, given its

economic weight, would be resisted for historical reasons; and it has been concerned that as such entities develop they could come to limit its freedom of manoeuvre. Its most important Pacific alliance being with the United States, it has not wanted any commitments to evolve that could ever complicate that alliance or diminish America's role in the region.

China's rise has, however, changed the situation, and promises to do so even more in future. If any sort of East Asian community analogous to the European Union emerges, then Japan cannot afford to watch it becoming a platform for Chinese power. Moreover, the case for more regional co-operation and even integration is increasing with the rising interdependence of the region's economies. So, at the same time as its politics and public opinion are becoming more assertive and more independence-minded, Japan is also becoming more interested in taking part in and (it hopes) leading regional institutions. The first East Asian Summit, bringing together government heads from South-East Asia, China, South Korea, Japan, India, Australia and New Zealand, will be held in Malaysia in December. It will also be the first big regional meeting in which America has not been a participant.

That fact makes many Japanese diplomats almost as nervous as the Americans. But nurturing regional institutions must surely be the right policy for Japan. If China's economy continues to grow, there is no chance that Japan will be able to beat it in an outright contest for regional leadership—and any such contest would risk becoming destructive for both countries. A better strategy will be to use regional institutions and treaties to dilute China's influence, establishing a framework of rules and procedures within which both countries will have to operate but which also offers the chance for Japan to build alliances with other Asian democracies.

When comparisons with the European Union are made, it is often assumed that the right analogue for Japan is Germany, since both were defeated in 1945. But that does not feel quite right. Japan's situation is akin to Britain's in many ways, being in Asia but not entirely of it, and having a closer relationship with the United States than with its neighbours. Yet during the next few decades, Japan's ambition should arguably be to do what France once did successfully in Europe: to be the Asian country that aims to use regional institutions to give itself a greater voice in world affairs, and to prevent its hefty neighbour from pushing it around. Except, of course, that it will want to remain on friendly terms with the Americans.

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The ambiguity of Yasukuni

Oct 6th 2005
From The Economist print edition

A private war shrine with imperial status

AP

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No ordinary shrine

IF YOU visit the Yasukuni shrine in central Tokyo, as Junichiro Koizumi has insisted on doing once a year to loud protests in China and South Korea, it is hard at first to see why this memorial to Japan's war dead is so controversial. Every country commemorates its military dead; this shrine dates back to 1869 and is dedicated to the 2.5m Japanese who have died in wars or civil wars since 1853. Its name, bestowed upon it by Emperor Meiji in 1879, means “peaceful country”. Only once you hear that among the spirits venerated at Yasukuni are 14 class A war criminals who were executed after the Tokyo war tribunal in 1948, and whose names were added to the roster at the shrine in 1978, do worries start to set in. But it is the shrine's war museum, the Yushukan, which really sets foreign eyebrows rising: this is no mere place of prayer, but puts over a controversial view of Japanese history.

To concern expressed about the presence of those 14 spirits, the government's response is that, yes, this is regrettable but Yasukuni has been a private religious entity since 1945 and Japan's post-war, American-drafted constitution separates state and religion, so the government can do nothing about it. Besides, in the Shinto religion, the *kami*, or spirits, at a shrine are thought to be indivisible: the war criminals have been put among the 2.5m others rather like 14 drops of water might be put into an ocean.

The flaw in that claim of constitutionally mandated impotence is that Yasukuni retains a strong tie with the head of state himself, the emperor. No emperor has visited the shrine personally since 1975, but every year, during the two principal rites at the shrine in the spring and the autumn, an emissary from the emperor plays the central role. The archive at the shrine, which is where the names of the war dead are logged, was built with a private donation from Emperor Hirohito (now Showa) in 1972.

The museum has no such direct link to the emperor. But, as John Breen of London's School of Oriental and African Studies wrote in June in “Yasukuni Shrine: Ritual and Memory”, an article for the *Japan Focus* website, the Yushukan is not like most other countries' official war museums: it is a museum without mention of any enemies.

Its sole purpose is to glorify Japan's dead, but in doing so it tells a clear story about Japan's conquests in Korea, Taiwan and China and about the Pacific war in general: that they were heroic

efforts to liberate Asia. And it features a large exhibit about the one judge at the Tokyo war-crimes tribunal, Radhabinod Pal from India, who considered the tribunal illegitimate. On the shrine's website, when you click for the museum, a slogan appears: “The truth of modern Japanese history is now restored.”

Officially, that is not the government's view. Japan accepted the verdict of the tribunal when it signed the San Francisco peace treaty in 1951, and insists that debate about the war is an inevitable part of being a democracy. But the fact that this debate is being conducted not just by extremists but by a shrine associated with the prime minister and many other LDP politicians as well as with the emperor makes this ambiguous, to say the least.

One obvious solution would be to have another official memorial. Yet one already exists: a war cemetery at Chidorigafuji in Tokyo. There is also a big ceremony on August 15th every year at the Nippon Budokan, Japan's martial-arts centre, to commemorate the end of the second world war, which is attended by the emperor and the prime minister. The real problem lies at Yasukuni. For, private or not, it has a special status.

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Visions of 2020

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Japan's next 15 years are likely to be a lot sunnier than the last 15

Reuters

Rare and precious

EVERY so often, a slogan rings out: Welcome to the new Japan! It comes from any pundit or panjandrum wanting to claim that, in a country that to many seems so unchanging, some dramatic new trend can be seen. But it is usually misleading, or exaggerated, for Japan doesn't do drama (and that is not a comment on Kabuki and Noh), except when it feels under threat of invasion, as in the 1860s, or suffers a wartime defeat, as in 1945. The stock- and property-market crashes that began in 1990 were dramatic for those caught up in them, and certainly produced a sharp change in perceptions of Japan in the world as well as in Japan's perception of itself. But the social and political response was totally undramatic. The country muddled through, at first in denial but later with a host of incremental adjustments. Fifteen years on, the same party is in government with a big majority, society remains stable, and Toyota is the world's best car company. Anyone know the Japanese for *plus ça change, plus c'est la même chose*?

As this survey has argued, however, that too is misleading. Those incremental adjustments, in politics, corporate law, capital markets, financial regulation, labour law and practices, and much else besides, have altered the incentives guiding society, the economy and politics. In part, the effect has been to reduce the distortions, misallocation of capital and indiscipline that have for about two decades neutralised Japan's long-standing economic and social strengths: excellent education, co-operative relations inside companies and advanced technology. But also, over the longer term, such a gradual accumulation of many small reforms will lead the country in new directions, especially given the recent changes in East Asia and the world economy as a whole, and given its own changing demography. No one can really know where those directions might take Japan over, say, the next 15 years. But some guesses can be made.

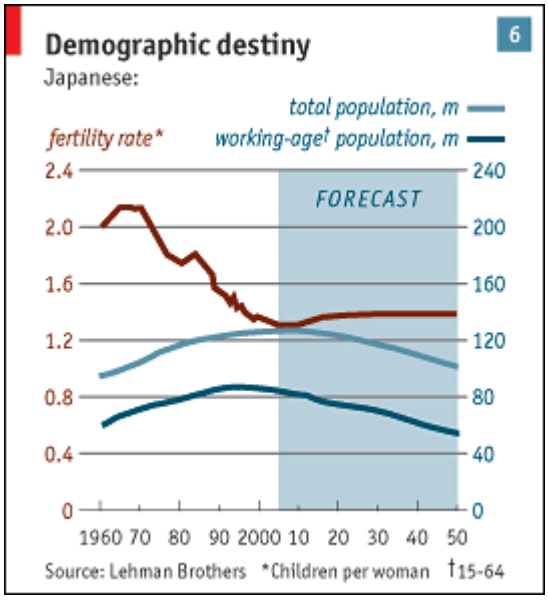
The easiest place to start is with demography. With birth rates having plummeted since the baby-boom of the 1950s and life expectancy having lengthened every year, the trend is pretty much fixed for at least the next 15-20 years: the government thinks the total population may have begun to shrink in the first half of this year, and it is certain to do so from 2007 onwards. That shrinkage will be slow, but with fewer children already entering the labour force and more people retiring, the working-age population (ie, aged 15-64) will fall by about 0.7% a year, says the Ministry of Health, Labour and Welfare.

If you extrapolate current trends well beyond 2020, you get quite startling numbers. The health ministry's central projection suggests Japan's population could fall from nearly 128m now to about 100m in 2050. Peter Morgan, chief economist in Tokyo for HSBC bank, reckons the ministry is being over-optimistic about birth rates, given that more and more women are marrying later or not at all. He thinks that a prudent projection for 2050 is actually a drop to 86m people. As Mr Morgan knows, however, demography is not destiny beyond 15-20 years. France, Scandinavia and above all America have shown recently that falling fertility rates can start to rise again. That could happen in Japan too.

The trouble is that the possible policy responses to boost the workforce and revive population growth could end up contradicting one another. With the labour force shrinking and ageing, companies and the government are both likely to try much harder to bring more women into the labour force and to use them in skilled and responsible positions. But the more that effort succeeds, the fewer babies are likely to be born. If the government tries to encourage women to have more children, on the other hand, fewer will be in the workforce in their 20s and 30s.

The way to meet both of those objectives would be to spend a lot more public and corporate money on child-care facilities, which are currently in short supply. The old way was to use granny, but today's and tomorrow's grannies want to spend their retirements travelling the world, and young women are not keen on having them around the house in any case. So there is bound to be some increase in spending on child care.

Awkwardly, the pressure for that spending will come at the same time as the public finances are being tortured in other ways. Ideally, you would not want to start dealing with all these problems when the budget deficit is already at 6.4% of GDP and gross public debt is 170% of GDP, as they have been in 2004-05. That is why the trend that Mr Koizumi has been busy accelerating, namely cutting back state spending, especially in wasteful public-works schemes and subsidised lending, is bound to continue. Space needs to be made in the public purse for child care, pensions and medical costs.



A shrinking labour force, with efforts to give women a bigger role, also means that the great worry of the past five years—that the rise of part-time and contract workers was producing a two-tier workforce—is likely to fade. There may be some more trimming of the protections given to regular workers in order to keep things flexible, but with labour scarce the new shifting army of irregulars, now 30% of the total, will surely fall in numbers.

Another solution that is often mooted to deal with both low fertility and scarce labour is immigration, which in conformist, homogeneous Japan has so far been tiny, except to take up the

nastiest of jobs. Most people's chief candidate for a bigger immigrant workforce has been health care, where a government desperate to reduce state medical costs ought to welcome cheaper Filipina nurses with open arms. The medical profession, protective of its own pay, has blocked that up till now. Eventually, cost pressures combined with a stronger economy are likely to break that resistance. But beyond nursing, nobody should expect a big rise in immigration. The social and cultural fear of it shows no sign of changing.

The potential of robots

The opening article of this survey cited the OECD's recent estimate of Japan's potential annual growth rate in 2004-10: just 1.3%. That number anyway looks low, as even during the country's stagnant decade of 1993-2003 the annual average growth rate was 1.1%. What it reflects, though, is an arithmetical calculation based on two numbers: the shrinking labour force just described; and the slow annual growth in productivity in the 1990s of about 2%, a whole percentage point less than in the 1980s. But the OECD's projection for productivity growth until 2010 is only a miserable 1.7% a year.

Here is a prediction, made with no arithmetic but much confidence: Japan's growth rate for the rest of this decade, and quite possibly for much of the following decade too, will be a lot higher than 1.3% a year. The country saw its productivity growth drop during the 1990s because it misused huge amounts of capital, and at the same time many companies hoarded labour rather than laying off workers. Now, with public-works schemes slashed, bank bad-debt accounts honest, shareholders and other ginger groups pressing public companies to boost profits and dividends, and the over-diversification of big companies a thing of the past, capital is bound to be allocated more efficiently. There is much catching up to be done in capital investment in any case that should boost productivity, and a much tighter labour market will force companies to seek ways to boost it even more.

One way that is already being talked about at the bigger manufacturing companies is the use of robots. Japan has long gone further than other developed countries in replacing workers with machines. An alternative is to replace Japanese workers with Chinese ones by opening factories in China, and some of that has been done. But the big electronics firms, for instance, are leery of that and others may become so too: Chinese workers' productivity is lower, they are harder for the Japanese to manage, there is a big risk of intellectual-property theft, and political relations between Japan and China are likely to remain scratchy. All this could well make robots and other machines increasingly attractive—especially if capital costs stay low.

No one can know, in an economy as large and diverse as Japan's, which industries are going to grow the most during the next 15 years. The game of picking winners became obsolete long ago. It is safe, though, to say that technology will still play a big part in investment and output growth in Japan. The country has been spending 3.1% of GDP on research and development even during the stagnant years, compared with 2.8% in America and an average of 1.9% in the European Union. Much of that is in advanced electronics, a field in which Japanese firms still lead the world. In future, there will be plenty too in nanotechnology, which takes the Japanese skill in miniaturisation down to the molecular level. Big efforts will also be made in biotechnology, though Japanese firms have a meagre record in that field so far.

A serious problem in the past 15 years has been slow growth in services businesses, which have failed to provide enough jobs and income to make up for those lost in metal-bashing. Deregulation has improved matters, but costs for telecoms and electricity remain high relative to those in other countries and there is still too little competition. A prime example is the vast wholesale-supply business: Jesper Koll, chief economist at Merrill Lynch in Tokyo, points out that of Japan's 380,000 wholesalers, two-thirds trade with each other rather than directly with a retailer or a producer.

The squeeze on those middlemen has begun. Seven-Eleven, for example, recently cut soft-drink prices at its convenience stores by more than 20%, at the wholesalers' expense.

Another services business that will need a kick up its bottom line is travel and tourism. All those pensioners are going to want to do more and more sightseeing, and rural areas are going to need the jobs that tourism brings. Although transport in Japan is top-notch, it remains pricey, however, and hotels are poor. An even bigger problem is that job-creation through public works has made so much of the countryside so ugly, thwarting job-creation through tourism. There are the beginnings of a movement among local authorities to tidy up their areas, dealing with what have become known as *keikan mondai*, or view problems. But there will have to be a lot more of that sort of thing if tourism is going to grow, especially from abroad.

Back to the politics of affluence

If the government is to become serious about raising productivity growth, which it surely must, competition will have to be strengthened, whatever the objections. Still, even with stronger antitrust enforcement and fresh deregulation to encourage more entrepreneurs, Japan is not going to become an American-style, free-market economy. You can tell by listening to one of its leading venture-capitalists, Yoshitaka Kitao of Softbank Investment. Despite his brash braces and combative manner, Mr Kitao talks a lot about the social obligations of companies. He thinks that young entrepreneurs like livedoor's Takafumi Horie, the notorious hostile bidder, are too greedy for money.

Over the next 10-15 years, Japan will have to begin to deal with the consequences of population decline. Faced with that burden, the country's GDP growth will never again reach the dizzy heights of the 1960s, 1970s and 1980s, nor be anything like as exciting as China's. But the more important measure is GDP per head, for that gauges living standards: if moderate GDP growth can be maintained alongside a slowly shrinking population, then GDP per head will rise quite nicely.

Just as neither the politics nor the economics of America after 1945 could sensibly be predicted on the basis of trends during the Great Depression of the 1930s, so the politics and economics of Japan ought not to be projected from its depressed past 15 years. With the important exception of the public debt, the excesses from that period now look to be gone. Politics and public policy will again face up to the demands of affluence, of labour shortages, of rising environmental concerns, of faltering universities and, above all, of a changing East Asian neighbourhood.

Given its huge electoral success on September 11th, much of that political debate can now be expected to take place within the Liberal Democratic Party, just as it has for the past half century, rather than between the twin poles of a two-party system. But it would take a brave man to predict that the LDP will still be in power in 2020. The lessons from Mr Koizumi, that electoral success requires charisma, a clear message and the promotion of change—rather than the old ingredients of money, a family name and a party machine—will not be lost on the younger generation in the opposition. Their time will come.

It might even come over the issue of foreign policy. The LDP's hawkish response to Chinese bullying has stoked up some nationalist feelings in Japan, but this remains a pacifist nation at heart. A bigger role in peacekeeping and humanitarian operations can be expected in future, but short of a grave international crisis there is little likelihood of Japan revising its constitution to unshackle its armed forces, nor of the country going nuclear.

Hence a final prediction for the Japan of 2020. In 15 years' time Japan will be a leading member of some sort of pan-Asian union, which will help it to keep China at bay. But it will still huddle closest to the United States, which will still have bases on Japanese soil. Some things never change.

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Retailing

Storm clouds over the mall

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Alamy

As consumer spending slows, rival strategies are being put to the test

"CONDITIONS on the high street are difficult, competition is intense and there is nothing to suggest this will change in the coming months." That was the message of Richard Baker, the chief executive of Boots, a chain of British chemists, earlier this summer. Since then, things have only got tougher. This week, Mr Baker announced the £7 billion ($12 billion) merger of his British retailing institution with a rival chain—a move widely seen as defensive (see article). With consumer spending declining in Europe and America, retailers are bracing for a thoroughly awful Christmas.

Shopkeepers are notorious Eeyores. But this time their fears may be well founded. Britain's economy grew at its slowest annual rate for 12 years in the second quarter, and a recent survey of retailing by the Confederation of British Industry has reported the fastest-ever year-on-year sales decline. In Germany's mired economy, retail sales in August fell for the third month in a row. In the same month, retail sales fell by 2.1% in America, led by a plunge in sales of gas-guzzling sports-utility vehicles. Consumer confidence in the United States is declining sharply (see chart).

A number of retailers have seen this slowdown coming. Lee Scott, the boss of Wal-Mart, the world's biggest retailer, has been warning for over a year that higher fuel bills are cutting into customers' spending. Sir Terry Leahy, who heads Britain's biggest retailer, Tesco, is also worried about rising fuel costs and increasing household debt. Yet compared with many smaller rivals, Wal-Mart and Tesco are still doing well: Wal-Mart's sales increased

by 10.2% to $76.8 billion in the second quarter to July 31st, compared with the same period a year earlier. And in its first half to August 13th, Tesco's sales were up 14% to £18.8 billion. It is the weaker players who are suffering. In the United States, Albertsons, the country's second-biggest grocer, has put itself up for sale after a long struggle against discount chains. Its 2,500 stores could fetch around $16 billion.

But it is not just other supermarkets that are feeling the pressure from the likes of Wal-Mart and Tesco. The giant supermarket chains are expanding into more product areas, such as clothing, health, beauty and electrical appliances. This increases the pressure on many high-street chains and department stores. Without the same buying power and economies of scale as the biggest supermarket chains, these retailers seem destined to suffer more from the present slowdown.

Change or checkout

How can a retailer ensure that it is among the survivors? The first thing companies need to do sounds easy, but is notoriously difficult: provide customers with what they want. To compete against the giants, retailers can specialise in a narrower range of products, often aimed at a specific group of consumers. Target, a more upmarket version of Wal-Mart, does this in America and also employs star designers to make products. Whole Foods Market, another successful American retailer, has become the leader in natural and organic products. But this is a moving battle. Wal-Mart is starting to offer more designer goods and organic produce.

Concentrating on specific regions can also help. Even successful retailers can stumble in new markets. Wal-Mart, for instance, has struggled in Germany against local discounters such as Aldi. Unless they are among the leaders in certain countries, big retailers are now inclined to throw in the towel. This week Tesco said it would swap, with a cash adjustment, its six stores in Taiwan for 15 hypermarkets in Slovakia and the Czech Republic owned by France's Carrefour. The deal allows each firm to quit markets where it is weak.

It is still not clear if any retailer will be able to dominate in all the big markets, especially China. However, a small group of world leaders is emerging, according to “Supermarket Wars”, a new book* by two retail experts, Andrew Seth and Geoffrey Randall. They list the leaders, so far, as Wal-Mart, Carrefour, Tesco and Aldi. Among the supermarket chains they believe will have no global clout are Albertsons and Sainsbury's—the latter in third place in Britain behind Tesco and Asda, which was bought by Wal-Mart in 1999.

Successful retailers also need to win the trust and confidence of consumers, either through pricing or service. Building trust means consumers will give a retailer the benefit of the doubt when it introduces new lines or own-branded products. So they have been happy to buy things such as DVD players, microwave ovens and clothing from supermarkets. Nowadays it is becoming easier for retailers to source high-quality products globally and brand them as their own.

Such changes in the supply chain can transform an industry, says Nick Greenspan, who leads the European retail practice of Bain & Company, a business consultancy. He cites fast-fashion as an example. Instead of long supply lines with garments ordered months in advance from China, some successful European retailers, such as Spain's Inditex (which owns Zara) and Sweden's Hennes &

Mauritz, order fewer lines more locally. Production is more expensive, but garments are in the shops within weeks and so are closer to the latest fashion trends. And stock is not replenished, but replaced with new lines. According to Bain, the profit margins and revenue growth of fast-fashion retailers greatly exceed those of many other chains.

Finally there is the internet, which every year takes a bigger share of consumer spending. Online sales of general merchandise in America will exceed $100 billion this year, according to Forrester, a research company. Carrie Johnson, Forrester's e-commerce specialist, predicts that will double by 2010, by which time more than half of all computers will be sold online, along with almost a quarter of cosmetics, 29% of small electrical appliances and more than 10% of clothes.

Yet the importance of the internet goes beyond cyberspace. A website can also drive in-store sales. Successful retailers are linking the two. Wal-Mart, for instance, is beefing up its website, which now allows customers to send in digital pictures and order prints to be picked up in an hour from a local store. And because big retailers can build virtual stores even bigger than their bricks-and-mortar ones, the breadth of products on offer is growing enormously. Online or offline, it will not be a happy Christmas for many retailers.

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Boots

A new prescription

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A retailing icon merges

THEY were the bastions of the British high street: Marks & Spencer, WH Smith and Boots. But now everything they sell can be found in supermarkets, sometimes more cheaply and often more conveniently—especially if it can be picked up with the weekly food shopping. This week Boots became the first of the trio to seek salvation in a merger.

Takeover speculation has swirled around all three. Marks & Spencer, a store chain once renowned for quality clothes and delicious food, fended off a hostile bid last year. Like WH Smith, a newsagent that also sells books, stationery and DVDs, Boots has been trying to restore its fortunes under new management, and concentrating harder on its core health and beauty businesses, instead of a rag-bag of products that have, at times, stretched from sandwiches to baby clothes and home wine-making kits. Richard Baker, its chief executive, was brought in two years ago from Asda, a British supermarket chain owned by America's Wal-Mart.

Provided the deal goes ahead, Boots will join in an all-shares merger with Alliance UniChem, a London-based group formed in 1997 by the merger of a British pharmacy chain and a Spanish firm. The combined group, to be known as Alliance Boots, will have almost 3,000 retail outlets in Europe, an extensive distribution system and combined sales of more than £13 billion ($23 billion).

The two companies believe the merger will bolster their businesses, result in cost savings and enable further international expansion. Pharmacy chains that also offer other goods can be successful, although it depends on the execution. America's Walgreens, for instance, is growing rapidly with almost 5,000 stores. But it has become as much a convenience store as a pharmacy. It also has a strong online business and drive-through outlets.

Analysts are unsure if the new Alliance Boots will find similar success. Boots is suffering from years of “decay and neglect” as well as over-pricing, says Richard Ratner, head of equities research at Seymour Pierce, an investment bank. “It's a short-term fix,” he adds. “Long term, they still have a problem.”

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Economist.com BUSINESS

Coca-Cola

In hot water

Oct 6th 2005
From The Economist print edition

The world's biggest drinks firm tries to fend off its green critics

Get article background

“WATER is to Coca-Cola as clean energy is to BP.” So declares Jeff Seabright, Coca-Cola's manager of environmental affairs, when asked about the firm's new global water strategy. The fizzy-drinks maker unveiled that strategy as part of its annual environmental report, released this week. “We need to manage this issue or it will manage us,” says Mr Seabright.

At first sight, the analogy with oil may seem odd, but it is not so far-fetched. Big Oil has long been the target of activists clamouring for action on global warming. BP stole a march on its oily brethren by accepting that climate change is a real problem, making smallish investments in clean energy, and grandly proclaiming itself “beyond petroleum”.

Coca-Cola has also been targeted by activists, but over the issue of water rather than energy. The firm has been hit hardest in India. First, experts from Delhi's Centre for Science and Environment, a green think-tank, tested various soft drinks and determined that they contained high levels of pesticide. It turned out that Coca-Cola was not the cause of the problem. But its inept handling of the accusations left the firm exposed to a much more damaging allegation: that it is aggravating the growing global problem of fresh-water scarcity. An ongoing controversy in India concerns allegations that some of the firm's bottling plants use too much water in drought-prone areas, thus leaving poor local villagers with too little. Amit Srivastava of the India Resource Centre, a Californian non-governmental group, has been using the Indian controversies to stoke an international grass-roots campaign against Coca-Cola.

The firm brags that it operates in 200 countries—“more than the UN itself”, says Mr Seabright. But Coca-Cola's global reach and iconic status make it an easy target. Mr Srivastava points with glee to recent decisions at a handful of university campuses in America and Britain to suspend or challenge its contracts on ethical grounds.

Worse may be in store, if some have their way. Corporate Accountability International (CAI), an activist group best known for organising a noisy boycott of Nestlé (for selling infant milk powder in countries without reliable access to clean water), now has its sights set on the world's largest producer of non-alcoholic drinks. CAI turned up at Coca-Cola's last shareholder meeting to grill the firm's management over the water issue. Kathryn Mulvey, CAI's boss, is concerned not only about its fizzy-drinks divisions but also its newish and booming bottled-water business. Echoing the sentiments of other campaigners, she insists that the “misleading marketing campaign” for the bottled water needlessly undermines confidence in tap water, and amounts to the “commodification of something that should not be bought and sold.”

Company officials argue that they started measuring and improving their use of water long before its troubles in India. The firm improved its water efficiency by 6% between 2003 and 2004. In 2002, it took 3.12 litres of water to produce one litre of final product (as much water is used to

clean the assembly lines, flush out glass bottles, and so on). In 2004, that global average came down to 2.72 litres. Mr Srivastava is not impressed: he grouses that it is “ridiculous that a firm that calls itself a ‘hydration company’ should waste so much water; most of it does not even end up in the product.”

To improve that situation, Coca-Cola has just completed a detailed assessment of the “water risks” to its businesses and their local communities. Going plant by plant, the firm's boffins have calculated local water-scarcity ratios, depletion levels for local aquifers, water needs for the local plant, and so on. With this new information, the firm is now setting local targets for improving each plant's efficiency of water and energy use. Mr Seabright explains that before this new study, the firm tried to impose “one-size-fits-all” global targets which local bottlers (who are often not owned by Coca-Cola) refused to accept.

Coca-Cola is also working with non-governmental groups such as the World Wildlife Fund and CARE, as well as UN agencies, in an effort to burnish its image. In India, it is now promising to capture enough water via “rainwater harvesting” (an age-old technique for capturing monsoon run-off) to offset all of its water use by 2006. Even the deeply sceptical Mr Srivastava concedes that “if this company were really not to put any strain on local resources then it would be a different matter. Let us see if this is just greenwash.”

The accusation of “greenwash”—environmental window-dressing as a front for business-as-usual—has also been hurled at BP. But there the similarities between Coca-Cola and BP end, for the question of water is far more important to Coca-Cola than the issue of climate change is to BP. That is because if oil and gas run out, or are deemed too dirty to use one day, BP could still peddle ethanol or hydrogen fuel; it is, in the end, an energy company. Coca-Cola, on the other hand, simply would not exist without water. So while BP may yet see life beyond petroleum, Coca-Cola will never get Beyond Water.

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Advertising

A hellish controversy

Oct 6th 2005
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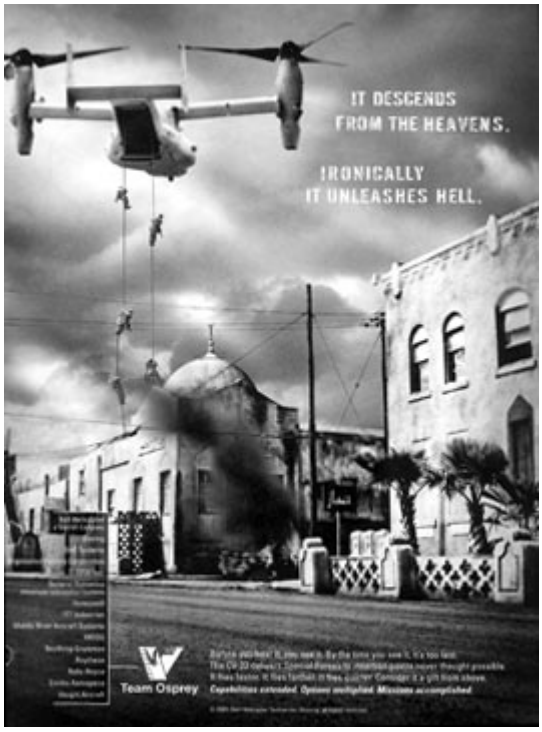
Boeing and Bell Helicopter get into trouble with an ad

AN AD for a revolutionary new helicopter has caused a row in America. A computer-generated picture shows an Osprey aircraft (which can fly like a plane and hover like a heli) above a mosque, with soldiers being lowered down on ropes onto the roof. The copy says “It descends from the heavens. Ironically it unleashes hell.” It also says “Consider it a gift from above.” The ad was intended to show off the ability of the aircraft to get soldiers into tight spots, such as areas where there is house-to-house fighting.



Let me re-phrase that

The offending picture first appeared over a month ago in the *Armed Forces Journal*. When senior managers at Boeing and Bell saw what had been put together by their Texas advertising agency, they immediately withdrew it from the magazine and from a number of other publications where it had been booked to appear.

But last week it was re-published, in error, by the *National Journal*, causing an outcry from the Council on American-Islamic Relations, an Islamic civil-liberties pressure group in Washington. Its fear was that the ad conveys an impression that the war on terror is in fact a war on Islam. Both Boeing and its joint-venture partner, Bell Helicopter, have said in statements that the ad was ill-conceived, offensive and should never have been published. It seems the Bell executive who cleared the ad for publication was not authorised to do so.

The companies have orders worth $19 billion for the aircraft, which has had a long and troubled development, with three fatal crashes of early models. Their prompt response may limit the damage to them, but it might not stop extremists using the whole episode as anti-American propaganda. For such purposes, it is indeed a gift.

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Economist.com BUSINESS

Designer glasses

Looking east

Oct 6th 2005 | MILAN
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An Italian success story

"ABOUT 90% of the Chinese population is myopic," points out Andrea Guerra, chief executive of Luxottica, the world's biggest maker of shades and prescription glasses. Chinese short-sightedness is one reason for Luxottica's second takeover in China since 2003. On October 4th, the company announced the acquisition for about €30m ($35.7m) of Ming Long Optical, the largest optical chain in Guangdong, in southern China. Adding to the company's presence in Beijing and Hong Kong, it will make Luxottica the leading high-end eyewear retailer in China.

At a time when many obituaries are being written for corporate Italy—as the country's firms struggle to cope with low-cost competition from Asia—Luxottica is one Italian company that is thriving in the global marketplace. Last year, the firm had total global sales of €3.2 billion. Because it specialises in high-margin goods, with an emphasis on craftsmanship and design, it still manufactures 85% of its production in Italy. But less than 5% of its sales are at home. The backbone of Luxottica's business is its own brands: Ray-Ban sunglasses, acquired in 1999, account for some 15% of the group's sales. But it also produces under license for Chanel, Prada, Bulgari and other luxury-goods firms.

Since the firm was founded by Leonardo Del Vecchio in 1961 in Belluno, a province in the north of Italy, it has thrived through mainly American takeovers. In 1990 Mr Del Vecchio listed his firm on the New York Stock Exchange. Five years later he branched into retail with the takeover of LensCrafters, the biggest optical retailer in America. This was followed in 2001 by the acquisition of Sunglass Hut, the world's leading retailer of sunglasses. Last year Luxottica took over Cole National, another big American retailer.

The integration of retail and manufacturing was a revolution in the industry, says Davide Vimercati at Kepler Equities in Milan. Today, retail generates more than two-thirds of Luxottica's revenue. Its retail arm is also the big difference between Luxottica and its archrival Safilo, another maker of sun and prescription glasses based in the north of Italy. The two firms are roughly equal in size in manufacturing, but Safilo's 50 shops pale in comparison with Luxottica's nearly 5,500 retail outlets, the vast majority of them in America.

China is Luxottica's next big challenge—a move that should expand sales, while lessening its dependence on America. Mr Guerra wants to conquer as much as possible of the "premium" segment, the market for glasses that cost $50 and more. This is ten times more lucrative than the trade in cheaper specs. Flavio Cereda, an analyst at Merrill Lynch, thinks that in a few years time Luxottica will double the number of its shops in China to 500.

Next year Luxottica's all-Italian 12-member board will probably become more international when some members' terms expire. The modernisation of the group began when Enrico Cavatorta, the chief financial officer, and Mr Guerra joined in 2002 and 2004 respectively. Until then Mr Del Vecchio ran the company pretty much single-handedly. Today, Luxottica's founder, who is 70 years old, has no operational role as chairman, although as owner of 70% of the company's stock

he remains very involved. None of his four children works for the company. Managing his succession will be the last step in the transformation of an Italian family company into a true multinational.

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Economist.com BUSINESS

Pharmaceuticals in South Africa

Aspen's upward slope

Oct 6th 2005 | JOHANNESBURG
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Can South Africa's top generics manufacturer become a global giant?

Reuters

A generic problem

THE number of South Africans with HIV-AIDS is tragic and alarming. The country has over 800,000 people who need treatment—but only about 100,000 of them are getting it. That is a huge social problem, but it is also a big challenge for business. Aspen Pharmacare is the local firm that is doing most to supply the market with the generic drugs South Africa will need. It now has ambitions to do the same for the rest of Africa—and then to expand into the market for generic HIV-AIDS drugs in the United States and Europe.

Founded in a suburban house in the coastal city of Durban in 1997, Aspen has grown at an average of over 40% a year and is now South Africa's leading drugmaker. Last August it announced annual revenues of 2.9 billion rand ($467m) and net profits of 494m rand. Its success is associated with the rise of generic medication. Both the government and health insurers—keen to keep medical costs down—have pushed for generics against the more expensive patented drugs. As a result, over 40% of prescribed drugs in South Africa are now generics.

The government and local pressure groups have arm-wrestled with the pharmaceutical multinationals over antiretrovirals (ARVs)—the drugs used to fight HIV-AIDS. As a result, companies such as Merck and Eli Lilly have licensed local manufacturers to produce their patent-protected drugs. The first South African company to obtain licences to produce anti-AIDS drugs still under patent, Aspen now offers six different ARVs. Last March, it won the lion's share of the government tender for ARVs.

In its quest to build up volume, Aspen—which still makes 80% of its profits in South Africa—is now planning to spread its wings elsewhere. It will supply the Clinton Foundation and the Bush administration's AIDS relief programme, both of which aim to spend millions of dollars on drugs for Africa. Over the long term, Aspen hopes to supply ARVs to the more lucrative American market once patents expire there.

Will Aspen pull it off? Its focus on specialised niches, the stamp of approval from important foreign regulators such as America's Food and Drug Administration, and the ARV contracts it has already bagged certainly put it on the right footing. It already has a successful operation in Australia.

Providing treatment to the many AIDS-afflicted Africans, however, is far more complicated than simply supplying drugs, and although the market is large, the uptake may be very slow. Competition in developed markets such as the United States is also far fiercer than in South Africa. Companies as far afield as Ireland and India are also expanding aggressively into the generics business. Aspen has managed to dominate its local market, but replicating its success abroad is likely to be much harder.

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Economist.com BUSINESS

Internet geopolitics

Gulliver's travails

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The battle to control the internet

SINCE the internet was created in the 1960s as a military-research project, America has co-ordinated the underlying infrastructure. But other countries are increasingly concerned that a single nation enjoys such power, and want to place the internet in the hands of an inter-governmental organisation—something America says might hobble the network.

At a diplomatic conference last month in Geneva to prepare for the United Nations World Summit on the Information Society, taking place in November, vocal critics such as Brazil, China and Iran led the opposition to America's control. On September 28th, the European Union abandoned its support for the current system and proposed a new, governmental approach, leaving America more isolated than ever.

Although the internet is largely decentralised and so difficult to regulate, the domain-name system is one of the few levers by which it can be controlled. Today, the internet is managed by a private-sector group called the Internet Corporation for Assigned Names and Numbers (ICANN), which America helped to set up in 1998 and still oversees. ICANN already has an international board of directors and a governmental advisory committee, but many non-Americans want to strengthen the role of governments.

The EU proposal, announced by Britain, which currently holds the EU's rotating presidency, was intended as a compromise between the UN supporters and America. It would create a new organisation to set policies over distributing routing numbers, creating new domains and the like. Because of its role as chair, Britain, usually America's closest ally on internet issues, had to stay neutral and could not beat back calls by Denmark, France, Spain and the Netherlands for greater government influence over the internet. After the announcement, Brazilian and Iranian delegates rushed to congratulate British officials, whose faces dropped when they realised the EU policy was being lauded by America's loudest opponents.

If ICANN already has a degree of government representation, why is a new organisation needed? Many of the arguments advanced come down to suspicion of America, and fear that ICANN is a tool of American hegemony. But another reason is that, although today the internet's address system identifies digital devices, in future it may be extended to encompass objects (through melding addresses with radio-frequency identification tags), location (via global-positioning satellites) and even individuals.

Meanwhile, countries demand sovereignty over their two-letter national address suffixes, which due to a quirk of history still ultimately reside under American control. Such concerns—which are political as much as technical—call for greater government involvement, or so the argument goes. All governments calling for change repeat the mantra that the new system would be a “multi-stakeholder” process that includes industry and civil-society groups.

However, the disingenuousness of the position was made clear during the meeting last month in

Geneva. Some countries demanded that groups representing business and public-interest causes be thrown out of the room when governments drafted documents for the summit in November. In one instance, delegates from China and Brazil actually pounded on tables to drown out a speaker from industry.

To break the impasse, some countries are trying to devise a compromise before the summit that will temporarily appease all sides. America has endorsed a proposal that would create a forum—devoid of formal powers—to discuss these matters. This will enable the issue to remain on the diplomatic radar after the UN summit. Indeed, the real battle will come in 2006 when America's contract with ICANN comes up for renewal and there is a big conference of the International Telecommunication Union, a UN body that aspires to fill ICANN's shoes.

Ultimately, the political squabbles are overshadowing more important things that could improve the lot of internet users, such as widening access to the internet and using technology for development. The good news from the UN meetings is that governments increasingly understand the importance of technology to society. The bad news is that the internet risks becoming suffocated in their embrace.

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Economist.com BUSINESS

Online music

Calling the tune

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Music firms are emboldened, but risk strangling the golden goose

Get article background

THE music business has long wailed that internet piracy is destroying its business. Now, it is fighting back on two fronts—first, by driving illegal operators out of business; then by driving as hard a bargain as possible with those firms selling legal downloads. Indeed talks between Microsoft and the major music firms have just broken down because the software company thinks the music business is demanding unreasonable levels of royalties.

Things are going better for the major record labels on other fronts. Last week the founder of a popular “peer-to-peer” (P2P) file-sharing program, Sam Yagan, told a Senate committee that his company will soon stop operating in its current form. He explained that eDonkey—which accounts for around half of all P2P traffic—can no longer afford to fight the music industry in the wake of the Supreme Court's ruling in June against two other P2P firms, Grokster and StreamCast, which declared that such applications are illegal if they induce users to violate copyright.

As expected, the music industry is now using its legal victory to hound commercial P2P operators out of business. Last month the music industry's trade body sent them threatening letters. WinMx, another P2P network, appears to have shut down, while eDonkey says it plans to start making its users pay for music. Grokster is reportedly on the verge of selling itself to a company called Mashboxx, which has a similar strategy to go legitimate. In Australia last month, a court ruled against Kazaa, another popular file-sharing service, and ordered it to use filters to stop the trading of copyrighted content.

Nobody, however, including executives at the major labels, believes that file-sharing is defeated. When the industry forced Napster, the first big file-sharing network, to shut down in 2001—it has since relaunched as a fee-based service—a host of free alternatives sprang up immediately, and that is what will now happen again. Because of the Supreme Court's ruling, says Mr Yagan, the new P2P services will simply move offshore and underground, and will offer more anonymity. In fact, the Supreme Court's decision is likely to encourage a move towards free, “open-source” P2P applications. Since they do not make money from advertising or bundling software, they are less vulnerable to the accusation that they are illegally inducing piracy for their own benefit.

In the first half of this year, digital-music sales from mobile-phone “ringtunes” and legal download services such as Apple's iTunes more than tripled compared with last year, and now represent 6% of total music revenues, according to industry estimates released this week. That rapid growth has restored confidence to the music industry, as have its victories in court.

So much confidence, indeed, that some of the major labels are urging Apple's iTunes service—the epitome of success in online music sales so far—to shift to variable (ie, higher) prices from the consistent $0.99 per track it currently charges in America. That would be a mistake. Despite its rapid growth, the legal market for music on the internet is still in its infancy. Apple's boss, Steve

Jobs, believes that higher prices would stifle legal sales and encourage P2P-based piracy. Microsoft might even deserve better treatment, too. Since the major labels' legal stick will never be completely effective against P2P, it is vital that they also offer an attractive carrot.

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Economist.com BUSINESS

Face value

The life and soul of the internet party

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Jason DeFillippo-Technorati

David Sifry, the founder of Technorati, is betting on a change in the nature of the internet

DAVID SIFRY'S epiphany occurred when he read “The Cluetrain Manifesto”, a book published in 2000 that quickly became a bible in certain Silicon Valley subcultures. Its main thesis is that “markets are conversations” among humans who use language that is “natural, open, honest, direct, funny and often shocking” and above all “unmistakably genuine”, whereas companies and governments are stuck in “the humourless monotone of the mission statement, marketing brochure, and your-call-is-important-to-us busy signal.” But liberation is at hand. The internet, by amplifying the genuine conversations, will make a laughing stock of all those using the monotone.

The manifesto struck a particular chord with Mr Sifry, as he pondered the shortcomings of his then passion—an electronic mailing list that he was sending around, tailored to ultra-geeks. “Mailing lists suck,” he says, with the benefit of hindsight. They don't let the sender or the readers see what is being said about them; they provide no window into the conversations that follow. Then, in 2002, Mr Sifry discovered the then-new medium of blogs—personal online journals, linked to other blogs and information on the internet. He dumped his e-mail list and started blogging. But he was frustrated because the most popular internet search engine, Google, was no help, when he “wanted to find out who was linking to me.” So he started a new company.

Technorati is a pioneering search engine for blogs, which allows the surfer to connect to online chatter on topics that might interest him—top topics this week, included Harriet Miers and Ajax football club. Like all search engines, Technorati makes money by selling little text advertisements next to the results of relevant searches. But, as Mr Sifry sees it, his firm is much more than a new sort of search engine—it is an expression of a change in the sociology of the internet. Most people

have over the past decade learned to think of the world wide web as a gigantic sort of library, with “pages” and “directories”. This explains the dominance of Google and Yahoo!, which have become the world's preferred librarians. In fact, both are making this role increasingly explicit. This week, Yahoo! joined several universities and archives to begin digitising old books in (physical) libraries so that they can be searched online. Google has similar plans.

As librarians, Mr Sifry acknowledges, Google and Yahoo! are “brilliant”—he has no intention whatsoever of competing with them in general web search. His idea for Technorati is subtly different, but has huge implications. Mr Sifry starts out with a metaphor for the web not as a library but—slipping into some technical argot common in Silicon Valley—“a big-ass threaded conversation”. Or, more poetically, a “river of human chatter”, constantly joined by other creeks and brooks and ever flowing. And whereas a library is by tradition a place where people whisper, Mr Sifry's internet is a cheerfully noisy place.

Mr Sifry's internet is a cheerfully noisy place

Technorati is therefore very different from ordinary search engines. Google and Yahoo! operate by “crawling” as many web pages as possible, making copies and putting them into an index, scoring and ranking them, and finally pushing them to web surfers who have typed search keywords into their browser window. Because of the time this takes, any snapshot of the web available through these search engines is between one and two weeks old—hopelessly late in the context of ongoing conversations. Technorati, however, does not crawl blog pages but listens for notifications—“pings”, in the jargon—from the blogs whenever they are updated. This means that Technorati's window into the subculture of blogging is only seconds or, at worst, minutes out of date. Technorati currently tracks about 19m blogs in this way, with an average of ten new “posts” (ie, updates) and one entirely new blog added, every second.

Mr Sifry's web-as-conversation metaphor is no longer eccentric. In fact, it is receiving the sincerest form of flattery (imitation) from the big librarians. In September, Google also unveiled a search engine for blogs (to decidedly mixed reviews), and Yahoo! is poised to launch its own. Mr Sifry says he is unintimidated by the arrival of these giant competitors. “Architecture follows from metaphor,” he proclaims grandly, and Google and Yahoo! just started out with the wrong metaphor. Tracking the web's conversations has only so much to do with algorithms, which is Google's prowess, and more with sociological insight—who responds to which blog, who recommends or snubs whom.

This, in fact, is what may give Mr Sifry a competitive advantage. He is that very rare thing, a geek who can use his right brain (social interaction), in addition to his left (computer code). On the left side, his geek credentials are impeccable. He has a degree in computer science and has been founding start-ups in Silicon Valley for a decade, dealing mostly with such nerdy obsessions as open-source software and radio-spectrum allocation. But rather than sporting a pocket protector and buck teeth, Mr Sifry has hints of a beer gut. While getting that computer degree, he boasts that he was “on and off academic probation” because he “always partied”. After college, he somehow found himself as the only *gaijin* in a Mitsubishi Electric factory in Japan. His speech is amiable Californian, peppered with “fucking” this and “fucking” that, in the excited tone of those surfing the nearby beaches, rather than the internet.

Mr Sifry has reason to be excited. Technorati's popularity is growing, as more and more bloggers get hooked on following the trail of their own conversations. Rivals are popping up with colourful names—IceRocket, DayPop, Bloglines—while Google and Yahoo! work on not being left out. Like everyone in Silicon Valley, Mr Sifry grows suddenly discreet when asked whether he would consider selling to one of them if the price were right. He may or may not. But whether or not Technorati will become the Google of the web's post-librarian era, Mr Sifry can at least rightfully claim that he started that particular conversation.

Gazprom

Russia's energetic enigma

Oct 6th 2005 | MOSCOW
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Polaris

As its tentacles spread along with its gas pipelines, Russia's giant energy company remains thoroughly mysterious

ACCORDING to the scuttle-butt, Vladimir Putin has a plan for when his second and—as Russia's constitution requires—last presidential term expires in 2008. Rather than changing the constitutional rules or becoming prime minister, Mr Putin may become boss of Gazprom, Russia's state-controlled gas monopoly.

The rumour is as telling as it may turn out to be fanciful. Gazprom is a leviathan. Last week, it agreed to buy most of Sibneft, the country's fifth-biggest oil firm, in what will be the biggest takeover in Russian history. But Gazprom's gas resources are already so big that its new subsidiary barely disturbs the company's profile. Gas will still constitute 90% of its production next year. One Moscow investment bank calculates that for oil to account for half of its output, Gazprom would have to buy the entire Russian oil industry. Last year, Gazprom produced 20% of the world's gas. It has 60% of Russia's gas reserves and 16% of the world's. If it were a country, its oil and gas reserves combined would rank only behind Saudi Arabia's and Iran's.

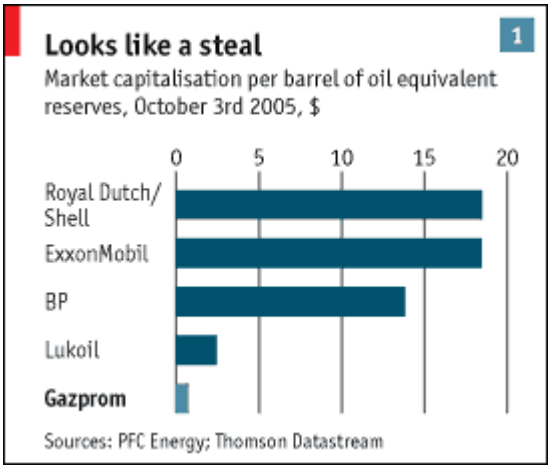
Russia's huge share of the world's gas makes it, rather than oil, the country's most important asset—and Gazprom its most important company. But many observers wonder whether Gazprom, which evolved from the old Soviet gas ministry, is really a company at all. Often, it seems more like an arm of the state.

The $13 billion Sibneft deal put Gazprom on the front pages of lots of western newspapers. But inside Russia, another Gazprom story has been captivating investors. It involves the supposedly imminent lifting of restrictions that circumscribe foreign ownership of Gazprom shares. This long-

drawn-out process seems to have been used to offset the damage done by the politically inspired destruction of Yukos, once Russia's biggest oil company. But the government's avowed precondition for it—an increase in the state's Gazprom holding to more than 50%—has now been met. Gazprom's share price has almost doubled this year in anticipation.

The prospect is enticing for two reasons. The first is technical. When the restrictions go, Russia's weighting in the emerging-market indices used by fund managers will jump dramatically, boosting the entire Russian stockmarket. Gazprom could become the world's biggest emerging-market stock.

The second is astronomically high energy prices. Russia has a lot of oil and gas, and companies that cuddle up to the Kremlin are the safest ones to invest in. Gazprom is chaired by Dmitry Medvedev, who is also head of the presidential administration. Putting aside the government's 51% stake, the company is extraordinarily cheap. Using the very rough measure of comparing the market capitalisation of top energy firms with their proven reserves, Gazprom is selling for a song (see chart 1).



Bullish Moscow fund managers argue that this discount cannot be justified and cannot last. The second point is almost certainly true. The first is more debatable.

Visiting the Kremlin, tourists are usually shown a giant, ancient bell that has never rung and a huge cannon that has never been fired. According to pessimistic analysts, Gazprom belongs more in this gallery of malfunctioning gigantism than among blue-chip global companies. As one pessimist puts it, Gazprom is a classic case of how a phenomenally valuable asset can fail to be a good investment.

Two parties are responsible: its management and the government. In 2001, Mr Putin appointed the hitherto little-known Alexei Miller as Gazprom's boss, reportedly with a brief to tackle the firm's legendary corruption. Mr Miller has recovered some valuable assets that had been “lost”. Corporate governance may continue to improve under extra shareholder scrutiny.

More murk than light

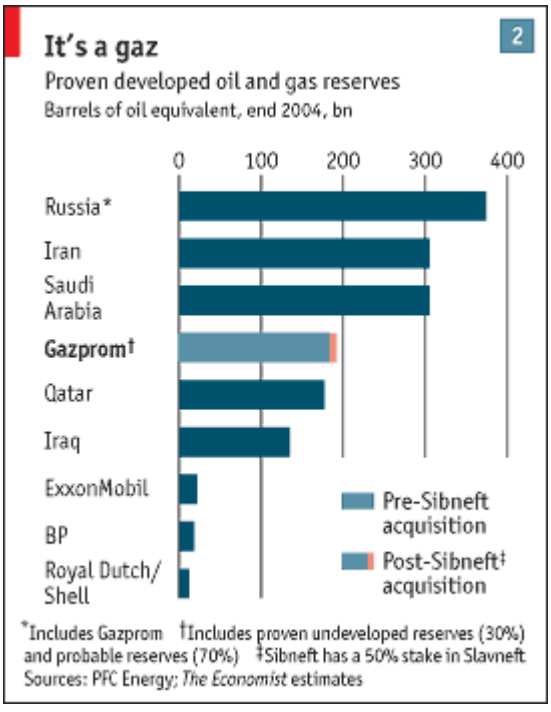
But at the moment, Gazprom remains a murky empire. Take, for example, the mysterious role that an obscure subcontractor plays in the delivery of gas from Turkmenistan to Ukraine, using Gazprom's pipes but depriving it of large profits. The Ukrainians are to blame, says Gazprom: “It's their gas,” says Sergei Kuprianov, Gazprom's spokesman, who also points out that Gazprom owns

half of the latest company to fulfil this odd function, whereas it owned none of the previous one. A spokesman for Naftogaz Ukrainy, Ukraine's national energy company, says Gazprom insists on the arrangement.

Consider also the extremely high cost of Gazprom's pipeline construction, compared with projects elsewhere in the world, and the strange intermediaries from which it buys materials. Mr Kuprianov says Gazprom's pipelines are bigger and the terrain harder: it is “one thing to build a pipeline in the steppe, another beyond the polar circle.” Vadim Kleiner of Hermitage Capital, a fund that tries to drive up Gazprom's share price by exposing graft, points out that Gazprom uses a “long chain of intermediaries and costs are rising fast.”

Closeness to the state does offer insurance against Yukos-style predation. But for minority shareholders, it carries its own risks. After Gazprom pays its taxes, which in 2004 accounted for around 8% of federal and regional tax revenues, the government's priority is long-term investment rather than paying dividends, which are puny compared with those of most Russian energy firms. State involvement also results in what observers tend politely to term “non-commercial behaviour”.

For instance, Gazprom says it is steadily unloading non-core assets—farms, holiday resorts and so on—that were either left-over from Soviet times or received as barter payments from customers thereafter. Yet it continues to make questionable acquisitions, given its existing assets and debt ($18 billion at the end of 2004, before it bought Sibneft). From a commercial point of view, for example, Gazprom's media business seems less than sensible. Why did its media arm recently buy a majority stake in *Izvestia*, a loss-making newspaper? In 2001, Gazprom also controversially took over NTV, a television station whose founder, Vladimir Gusinsky, was the first of the “oligarchs” to fall out with Mr Putin. Mr Kuprianov says the media division needed a newspaper to complete its portfolio. But why does Gazprom need a media arm at all?



The most important reason for Gazprom's share-price discount, however, is that it is obliged to sell the bulk of its gas inside Russia at regulated prices. Although prices have been rising relatively sharply since 2000, and are supposed to go up further as a condition of Russia's putative

membership of the World Trade Organisation, they remain low. The average wholesale price in Russia during 2004 was $29 per thousand cubic metres (tcm); for exports to western Europe, the average price was $140. The result is a sort of reverse dumping. Gazprom receives two-thirds of its revenue from the one-third of output that it sells abroad. It says it just about breaks even on domestic sales.

This situation is bad for Gazprom but has benefits for Russia, which is an enormous, cold and poor country. A swift hike to much higher tariffs, even if it led to more efficient energy consumption, would boost inflation. A lot of people might stop paying and get very cold (and angry) if they were cut off.

In return for its “handicap”, Gazprom enjoys two useful privileges. The first is control of the world's biggest pipeline network. (The idea of splitting transportation from Gazprom's production side, long talked about by reformers, has been more or less dropped.) Gazprom says that it has no incentive to keep independent gas producers out of its system, since the more independent gas sold in Russia, the more of its own it can export at higher prices. As evidence of its fair allocation of access, it points to the rising independent share of total gas production (14% last year). But, at the very least, Gazprom's grip on the routes to market lets it muscle its way into other companies' projects. Bosses of the independents agree on their need to have a “Gazprom strategy”, though they are understandably reluctant to criticise Gazprom's tactics in public.

Gazprom's other compensation is its monopoly on gas exports to countries outside the former Soviet Union. It justifies this on the grounds that competition between Russian suppliers would bring down prices and thus government tax receipts, jeopardising long-term projects. In economic terms, this argument has some merit, since Russia is more of a “price-setter” in the gas market than a “price-taker”, which it is in oil. But the export monopoly discourages the investment by other gas producers that Russia itself badly needs. Production at Gazprom's main gas fields in western Siberia has peaked, while domestic demand is booming.

Still, the export monopoly offers a different benefit: it guarantees the Kremlin's control over what, with the possible exception of nuclear weapons, has become Russia's most powerful foreign-policy tool, and its best hope of regaining lost clout.

Last month, Mr Putin and Gerhard Schröder, Germany's chancellor, presided over the launch of Gazprom's latest mega-project: a €4 billion ($5 billion) pipeline that will run under the Baltic Sea to Germany, Gazprom's biggest foreign customer, and thence, eventually, to Britain. Mr Putin again extolled the scheme's importance at the EU-Russia summit this week. Almost half of the European Union's gas imports come from Russia. European demand is expected to double between 2000 and 2030. Gazprom and the Russian government say that the Baltic pipeline is a useful way to diversify supply routes to a growing market (see map).

But things look very different in Kiev (and in Warsaw). Most of Gazprom's exports currently flow through Ukraine; much of the rest goes via Belarus and through the “Blue Stream” pipeline that crosses the Black Sea to Turkey. This accident of geography has been lucky for Ukraine, which has hitherto been able to parlay its transit role into cheapish gas for itself (the average price for sales to former Soviet Union countries last year was $54 per tcm). That leverage will be seriously diminished by the Baltic pipeline.

Of course, there are sound reasons why Russia's former vassals should pay the market price for Gazprom's gas—so long as prices and supply are determined fairly and transparently. This has not always been the case: witness, most famously, the brief interruption in deliveries inflicted on Belarus in February 2004 after Alexander Lukashenka, its tragicomic president, irked Gazprom and Mr Putin once too often. Yuri Yekhanurov, Ukraine's new prime minister, visited Moscow last week, amid talk of an imminent tripling in his country's costs. Both Ukraine and Georgia—another country that is unpopular in the Kremlin, and which lacks Ukraine's transit leverage—are urgently scrambling to find alternative sources of energy.

But for Gazprom, Europe is just the beginning. It has insinuated itself into the most developed of the hydrocarbon projects on Sakhalin island (see article), led by Shell, from which the first liquefied natural gas to be shipped to America (via Mexico) will be sent. Cost overruns on Sakhalin may explain why Shell is not among the companies Gazprom has shortlisted for inclusion in another mega-project: the exploitation of the vast Shtokman gas field in the Barents Sea, whose contents will also be liquefied and shipped to America from around 2012. Gazprom is also leaning on TNK-BP, an Anglo-Russian energy firm, for a cut of its Kovykta project north of China. And as Mr Putin said this week, Gazprom wants to be involved in the distribution of its products in the West. It has already bought up chunks of distribution networks in central and eastern European countries that are almost entirely dependent on Russian energy imports.

In short, how Gazprom behaves in future will be a key test of Russia's desire and ability to turn itself into anything resembling a “normal” country. So in a way, all those fund managers rushing into Gazprom are really buying shares in Mr Putin and his (eventual) successor. As Chris Weafer, of Alfa Bank in Moscow, puts it, “If the Kremlin had a stock-exchange listing, Gazprom would be it.”

Economist.com BUSINESS

Sakhalin

Energy island

Oct 6th 2005 | KORSAKOV AND YUZHNO-SAKHALINSK
From The Economist print edition

The trials of Russia's new petro-state

VISITING when the island was a tsarist prison colony, Chekhov wondered how anyone could survive Sakhalin's “povertyfoul weatherunchanging view of barren mountains, and the roar of the sea.” Although it now hosts Russia's biggest foreign investments, some things have not changed. The sea around the northern coast freezes for half the year, stopping tankers from reaching the offshore platform that in 1999 began pumping oil as part of the “Sakhalin II” project. Still, for Gazprom, Sakhalin was irresistible.

Last week, the consortium behind “Sakhalin I”, led by ExxonMobil, produced its first oil. But the most advanced and ambitious of the island's oil-and-gas developments is Sakhalin II, led by Royal Dutch/Shell. Two more platforms are being added; oil and gas will be piped onshore and then down the island in twin pipelines to an oil terminal and Russia's first liquefied natural gas plant (LNG is gas cooled to a fraction of its normal volume). The $13 billion Exxon-led rival scheme will send its oil across the Tatar Strait to the mainland, although apart from some local sales, it still seems unsure of what to do with its gas.

Sakhalin II has pre-sold 80% of the LNG it will produce over 20 years to Japan, South Korea and North America. Gazprom needed a share of these new export markets: it is getting it by swapping 50% of one of its Siberian fields for 25% of Sakhalin II. Most of that stake will come from Shell's 55%, although sources close to the deal say a slice will also come from Matsui, a Japanese partner, leaving Gazprom as the second-biggest participant. Shell will get new reserves to add to its books.

Unfortunately for Shell, the deal soured over the summer when Sakhalin Energy, the project operator, doubled its estimated costs to around $20 billion and LNG production was delayed until 2008. Under the terms of its agreement with the government, higher costs mean lower revenues for Russia.

Environmental oversights account for part of the miscalculation. “They planned the project as if they were planning for a new planet,” says Tatiana Serykh of the World Wildlife Fund. Pipeline routes from the platforms to the island had to be changed to avoid the feeding grounds of an endangered whale. New measures were needed to prevent the onshore pipelines from damaging the 1,000-odd waterways they cross. “If you say you're not doing any environmental damage, you're a fool,” says one engineer. Ian Craig, Sakhalin Energy's chief executive, says the local poachers do much more harm.

Energetic activists and the company seem between them to have addressed the gravest environmental worries. Social resentment on the impoverished island may be less tractable. Locals complain about damage to fishing, their most functional industry: in spawning season, salmon jostle at the mouths of Sakhalin's rivers. Islanders ought to be cross with Russia's government, which has decided to direct almost all of Russia's share of the Sakhalin II profits back to Moscow. But Soviet-era notions about the responsibilities of big enterprises, combined with despair at

getting anything from Moscow, mean anger focuses on the company. “They bring nothing to the town, except problems,” says the mayor of Korsakov, grim home to around 40,000 people and a stone's throw from the LNG plant. The even poorer indigenous reindeer-herders are said to be much less demanding.

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Economist.com FINANCE & ECONOMICS

China and commodity markets

From accelerator to brake

Oct 6th 2005 | HONG KONG AND SHANGHAI
From The Economist print edition

Imaginechina

The Chinese economy has driven a boom in commodity markets. It may be turning into a drag

Get article background

NOWHERE has China's growing economic influence been felt more powerfully than in the world's commodity markets. The country's enormous appetite for base metals, minerals and fuels has pushed their prices to new highs and created record profits for the companies that extract and process them. With China swallowing raw materials as fast as they can be dug up, some observers even talk of a “super-cycle” of extended high commodity prices.

However, the popular perception of China as an insatiable commodity-guzzler is now too simple. As the Chinese authorities have attempted to cool overheated parts of their economy, from construction to cars, consumption of some commodities has slowed sharply or even fallen. According to Dong Tao, chief Asia economist of Credit Suisse First Boston (CSFB), Chinese demand for oil has been just 2% higher so far this year than in 2004; demand for cement has been flat; and that for aluminium has declined by 5%. Analysts had been expecting growth of 10-12% for cement and 6-7% for oil and aluminium. Even though GDP growth still looks robust, at 9%-plus, Mr Dong thinks that “the economy is losing momentum perhaps faster than the market currently believes.”

Slowing demand has hit prices. It is also turning China into a net exporter of some of the materials for which it has until lately been scouring the globe. Take steel. So far this year the mainland has consumed about a third of world output (of 730m tonnes), and its demand is rising at an annual rate of 20% or so. But China's own production is expanding even faster, by around

30% a year. As a result, China, which last year imported about 15m tonnes, is likely to export as much as it imports this year and may have trade surpluses of 9m tonnes in 2006 and 13m in 2007, reckons Trina Chen, an analyst at CSFB. This swing has already helped to depress international steel prices. Domestic Chinese steel prices have fallen by a third from their peak at the start of the year.

China is also a growing exporter of aluminium. And its cement exports have nearly tripled so far this year. Although the base was small, this worries Taiwan Cement, a big producer on the island: no wonder, when the Chinese stuff is $50 a tonne cheaper. China's dependence on oil imports is waning too. As it expands its electricity grid, it is consuming less crude, because 70% of the country's power is generated from coal. Diesel generators, which account for around 40% of China's incremental oil demand, are being used less because China has fewer power shortages. This should eventually weaken one prop for global oil prices.

The extent and duration of China's weakening demand for commodities is hotly debated. “You have got to be careful about the China slowdown story,” warns Clinton Dines, chief executive of the Chinese operations of BHP Billiton, one of the world's largest mining groups, which has made a fortune selling to China. Demand for some commodities looks as strong as ever. One is coal, on which BHP Billiton is so keen that it could change its strategy of not investing directly in China and buy a local mine. Copper prices keep hitting record highs: China, which consumes a fifth of the world's supply, mostly for new power lines, increased its imports by more than 12% in the first eight months of the year. Uranium, for use in nuclear power stations, is also still in demand.

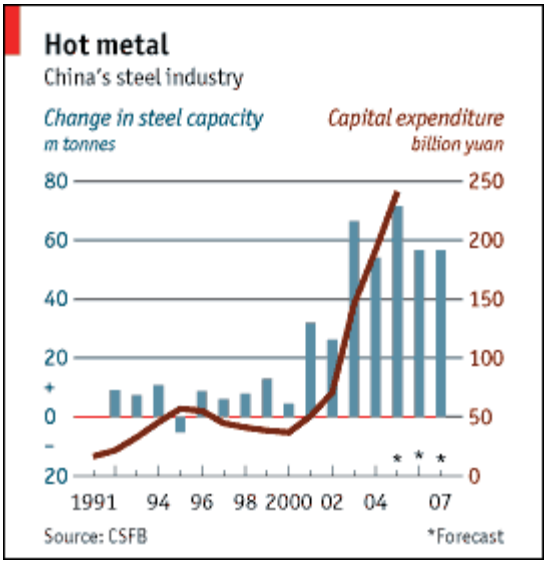
In other raw-material markets, the recent weakness reflects inventory corrections: aluminium consumption, for example, has dropped partly because carmakers have run down their stocks. But for some commodities, a new wave of demand may be gathering, as construction, the main driver of demand for steel, aluminium, cement and related goods, appears to be accelerating again—from growth of 10-15%, year on year, in the second quarter to almost 30% in July, according to UBS. This is in turn pushing up overall import volumes, where annual growth is now almost 10%, having touched zero early this year. The government seems less worried about the current round of building than the last, because wild borrowing seems to be financing less of it. Soon construction for the 2008 Olympics will also kick in.

Even so, Jonathan Anderson, UBS's chief Asia economist, says that he doubts a construction upturn could drive the annual growth of import volumes back to 35-40% and “make China once again the single largest growth driver of Asian (and global) trade and GDP.” Import growth, he thinks, will be constrained by slowing investment in fixed assets for heavy industries and by the excess capacity built up in the past three years.

This excess capacity is the main reason to expect more weakness in the mainland's demand for several commodities and hence in world prices. China's huge investment in production facilities for basic metals and materials increasingly will allow the country not only to satisfy its own demands but also to let any overflow wash into world markets.

Steel is the prime example (see chart). The capacity of China's 260-odd steelmakers could reach 390m tonnes by the end of 2005, up by 23% year on year, and maybe 500m tonnes by 2007. At a steel conference in Seoul this week, Nicholas Lardy, of the Institute for International Economics in Washington, DC, pointed to “massive, massive excess capacity” in China at a time when steelmakers elsewhere are curbing production growth. In aluminium, 20% of new smelter capacity in China is lying idle because of a lack of raw materials. Once that

comes on, CSFB estimates, supply could outstrip demand growth over the next two years—even though demand will be rising at a double-digit pace. China's exports next year could be 1m tonnes, twice what they were in 2004.



All of this will cause political headaches for the Chinese as well as economic upset for their trading partners. Until now, China's surging exports of manufactured goods have at least partly been balanced by its strong imports of raw materials. If it now starts to export commodities and basic goods as well, trade tensions can only worsen. Steel could follow textiles as the next flashpoint.

There are signs already. On October 3rd, America's International Trade Commission agreed that rising steel-pipe imports from China were causing "market disruption", a victory for American pipe producers who have been lobbying for protection. Recently, POSCO, South Korea's largest steelmaker, gave warning of China "turning into a threat" as South Korean shipyards develop an appetite for cheap mainland steel. And at the Seoul conference, Guy Dolle, chief executive of Arcelor, the world's second-largest steelmaker, painted a terrifying picture—for him, anyway—of a gigantic Chinese steelmaker, pushing out 150m tonnes a year.

Whether China's government will manage to consolidate the sector to this extent is questionable, given the strength of vested local interests. But that is not the point. The bogeymen are already being conjured. Both China and the rest of the world will find an end to the long commodities boom hard to handle.

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Economist.com FINANCE & ECONOMICS

Private equity and energy

Gusher

Oct 6th 2005 | NEW YORK
From The Economist print edition

A fortune has been made in private energy deals

NOT everyone is miserable about high energy prices. Many investors who were brave, clever or lucky enough to buy American energy companies two or three years ago, when prices were low and sellers were desperate, are in clover.

In the past few days, Chesapeake Energy has said it will pay between $2.2 billion and $3 billion for the vast gas reserves of Columbia Natural Resources. The seller, a private-equity affiliate of Morgan Stanley named Triana Energy Holdings, paid only $330m for Columbia in 2003. NRG, a power-generation company, has agreed to pay $5.8 billion for Texas Genco, another generator. The sellers are a group of private-equity firms, including Kohlberg Kravis Roberts, Texas Pacific, Blackstone and Hellman & Friedman, that bought Texas Genco only at the end of last year for just $900m (plus $2.5 billion in debt that will be passed on in the deal).

These huge returns show how a buyer's market has turned into a seller's one. “No one else could afford to buy them, and it was just before the price of energy and power took off,” says Charles Ober, manager of T. Rowe Price's New Era mutual fund.

Consider how badly off even the current buyers were. NRG was bankrupt between 2002 and 2003. Chesapeake's shares drooped to 69 cents in 1999; they now fetch around $38. As for their purchases, Columbia was bankrupt between 1991 and 1995. Its owner before Triana sold futures contracts at extremely low prices that could still cost as much as $775m to settle. Texas Genco has a similarly topsy-turvy story. It was spun off last year by CenterPoint Energy, another utility that had troubles in 2003. It might have gone to Reliant Energy, once a sister company of CenterPoint, which had an option to buy Texas Genco but let it drop.

Reliant was still reeling from an earlier purchase, from Goldman Sachs in 2002, which turned out to be rather expensive. It said this week that it was selling three New York City generation plants that were part of that deal for $975m, a loss of $160m, to another private-equity group. Clearly, some buyers and sellers are more adept than others.

These deals are just the visible tip of an active market. Several energy companies have recently made private placements, selling securities directly to institutions. Among them is Mariner Energy, an oil and gas exploration firm that until last year was controlled by Enron (and has been since by private-equity firms). Mariner does not release its results, but is said to be doing quite well.

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Economist.com FINANCE & ECONOMICS

American Treasury bonds

Among the missing

Oct 6th 2005 | LONDON AND WASHINGTON, DC
From The Economist print edition

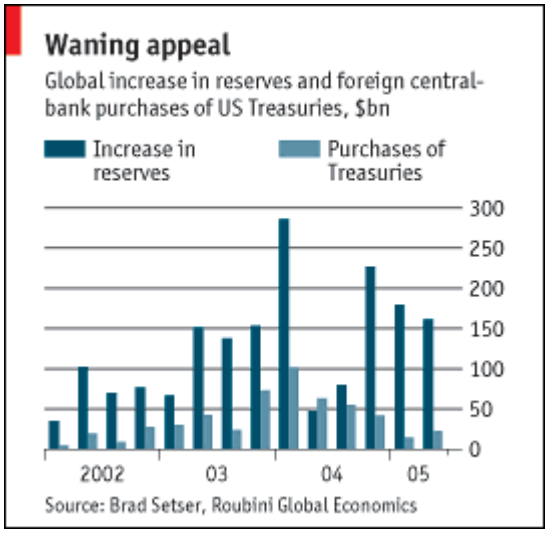
Behind the Treasury-bond market's recent ups and downs

THE Federal Reserve took to the pulpit in force this week to preach against the dangers of inflation. On October 3rd, the president of the Atlanta Fed gave warning that monetary tightening still had “a way to go”. The next day, his St Louis counterpart said the futures market was “reasonable” to price in the near-certainty of two more rises in the fed funds rate this year. The heads of the Dallas and Philadelphia Feds railed separately against inflation.

They almost managed to scare bond yields much higher. Ten-year Treasury yields touched 4.4%, on October 3rd, their highest in almost two months. News that input prices had risen sharply in manufacturing added to the gloom. Investors then broadly regained their nerve and despite more bad news about prices, this time in services, yields ended October 5th at 4.34%. That was still far above the 3.98% that they hit just after Hurricane Katrina.

What really drives yields? Fed-watching matters a lot at the shorter end of the spectrum. And concern about inflation is arguably the main determinant of long-bond yields. But the appetite of foreigners and especially foreign central banks—many of whom, the theory goes, have to buy Treasuries willy-nilly—has played a big role. What is pushing yields now: a reservoir of foreign official buyers desperate to recycle surplus trade dollars at any price, or the economic fundamentals, expectations, and law of supply and demand that drive most markets in most places?

The question has taken on a new urgency with what looks like the fading of foreign central banks' interest in Treasuries. Purchases by Asian banks, in particular, shot up in 2003 and 2004, financing America's fast-growing deficit. While official reserves are still piling up, foreign central banks' buying of Treasury bonds has plunged as the chart shows.



That is partly because the banks are getting nippier at managing their portfolios. They have been buying more of other things, mainly higher-yielding bonds issued by government-backed agencies such as Fannie Mae, the mortgage giant. Some, too, are choosing to buy in the secondary market abroad, which shows up in private rather than official flows.

This may be especially true of many OPEC countries, including those, such as Kuwait, with national wealth-management funds. (Just how the oil-exporting countries are deploying their soaring surpluses—some $400 billion this year, more, on the IMF's figures, than the surpluses of Asia's main economies—is far from clear, but their holdings of Treasuries are declining these days, says Bulent

Baygun, head of US fixed-income strategy at Barclays Capital.) On October 5th it emerged that Venezuela, perhaps for political reasons, had apparently transferred as much as $20 billion—most of its reserves—out of Treasuries and out of America.

Indirectly, central banks' diversification out of dollars may also be boosting private-sector demand for dollar assets. Moving more into euros, they are helping to push down yields in Europe. Private investors there are eyeing Treasuries with greater enthusiasm: the yield on the ten-year is now 1.2 percentage points above that on German bunds, the most since 2000. And the dollar has stayed stronger than almost anyone imagined. So while foreign official purchases of Treasuries fell in July, private flows increased sharply.

How much have central banks—and foreigners in general—kept down interest rates for the world's biggest borrower? Economists disagree. Alan Greenspan, the Fed's chairman, has suggested that the effect of official flows is “modest”. Brad Setser and Nouriel Roubini, of Roubini Global Economics, a consultancy, reckon that central-bank buying at its peak could have dampened Treasury yields by up to two percentage points. And a new paper by Francis Warnock and Veronica Cacdac Warnock, of the University of Virginia, published by the Fed, finds that if foreign central banks had bought no Treasuries over the past year, ten-year yields would be 60 basis points higher. If all foreigners had boycotted American bonds, the increase would be 1.5 percentage points.

Gerald Lucas, Bank of America's chief Treasury strategist, thinks the Warnocks' estimates are “exaggerated”. He reckons that the Fed's credibility as a dedicated inflation-basher has a lot to do with why long-term yields are low. The remarks by the tub-thumping quartet of Fed presidents will have done nothing to dispel it.

A curious new trend in the eurodollar-futures market, however, hints that interest-rate hikes may end sooner than most assume. Alex Patelis, of Merrill Lynch, points out that the market has begun to price three-month money two years from now more cheaply than three-month money in a year's time. There have been only four such inversions in 20 years, he says—and three were followed within two months by the end of a rate-tightening cycle. Is the market betting that Mr Greenspan's successor will be less hawkish than he has been?

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Economist.com FINANCE & ECONOMICS

Remodelling Allianz

Agent of change

Oct 6th 2005 | MUNICH
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The delicate business of reorganising Europe's biggest insurer

TURNING ideas into reality is never as easy as chief executives would like. In Germany, where workers are represented on company boards and “consensus” is a cardinal social principle, it can be a particularly delicate operation. Michael Diekmann, boss of Allianz, Germany's (and Europe's) biggest insurer, has a clear idea of how his company should be structured. Although it is global, he sees its home market as Europe. And instead of the current five product lines, he wants only three: insurance, asset management and banking (through a subsidiary, Dresdner Bank). His plan, though, is causing grief in Germany.

At home, Allianz's traditional strength has been its network of insurance agents. Almost every village from Bavaria to Brandenburg has an agent, whose window sports the firm's blue eagle and who plies only Allianz products. The agents have been best at selling property and casualty (P&C) cover but increasingly they have been urged to sell life policies and health insurance too. Until now, P&C, life and health sales have been run by different arms of Allianz. Last month Mr Diekmann said that one subsidiary would do the lot.

Replacing three client databases with one will save Allianz lots of back-office costs. The heavily unionised workforce, however, sees the idea as a potential job-destroyer. The agents too, although they live on commission, fear that the drive to cut costs will erode their business. Last month Allianz began to offer car insurance online at prices well below those it quotes to agents and independent brokers.

This week Mr Diekmann explained his thinking to agents at a get-together in Athens. Online motor-insurance, he argued, is aimed at young buyers in big cities, whom Allianz agents hardly touch (they do best in rural areas). Surely, he said, the agents would rather these youngsters bought one Allianz product and became potential clients for more, than that other insurers sold them car cover online instead?

Allianz's biggest problem at home is the stagnation of its P&C business (worldwide, P&C provides 58% of the company's operating profit; life and health supply 21%, asset management 12% and banking 9%). For example, sales of car insurance, one type of P&C business, have been heavily hit by the increase in oil prices. The German restructuring may be the right course of action, but the bosses have not yet said how many jobs it will cost. Allianz sources say that this is hard to predict because the growth of the firm's business depends on market conditions and the possibility of retraining back-office staff as salesmen.

All this shows how softly Mr Diekmann feels he must tread. It does not help that, as in all big German companies, workers' representatives have 50% of the seats on Allianz's supervisory board. Even though these cannot outvote the management, they can make life awkward. The unions already have an eye on works-council elections next March.

Last month Allianz it said would adopt the legal form of a Societas Europaea (SE), a European

creature, instead of a German *Aktiengesellschaft*, in order to effect a full merger with RAS, an Italian insurer of which it already owns 55%. An SE can have either a single, Anglo-Saxon-style board or the German two-tier model of management and supervisory boards. Allianz will keep two tiers, but wants to cut the membership of the supervisory board from 20 to 12. A change of system was never on: when converting to an SE, a firm with workers' delegates on its board can abolish them only by agreement. Fat chance.

Outside Germany, the merger with RAS will give Allianz a better hold over its businesses in Italy, Austria, Spain and Portugal, which will report directly to Munich rather than via Milan. It may later fold in another Italian subsidiary, Lloyd Adriatico. But it may be some time before Allianz carries out a similar merger with AGF, a French insurer of which it owns 60%. German cross-border merger rules favour the valuation of a court-appointed auditor over the relative market worth of the two companies. For AGF, the former would be so far below the latter that no minority shareholder would accept it.

The international bits of Allianz's reorganisation may in any case be less important than they appear. Cross-border sales of insurance are still not a reality, despite efforts to create a single European market for financial services. Allianz's SE status is likely to be approved by shareholders in February. But despite the firm's pan-European form, it will have to keep working country by country.

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IPOs in Germany

Solar flares

Oct 6th 2005 | FRANKFURT
From The Economist print edition

Once again, Germany's stockmarket feels the warm glow of new share issues

Get article background

AFP

Sunny outlook

DON'T get too excited—or nervous—about the flurry of small firms floating on the Frankfurt stock exchange. In the past week, two makers of photovoltaic panels, ErSol and Q-Cells, both from former East Germany, have enjoyed heavily oversubscribed initial public offerings (IPOs). The soaring oil price and the quest for alternative fuels are boosting demand for anything solar. Indeed, of the 13 IPOs in the past two years, four have had to do with solar energy.

Operators of closed-end investment funds (which invest in other companies' shares) are also proving popular. One, Interhyp, listed last week and was 30 times oversubscribed; another, HCI Capital, made its debut this week and could have been sold four times over. A third, Lloyd Fonds, is due to float on October 28th. And Tipp24, a fast-growing online-lottery firm, plans to come to the market on October 12th.

Brokers say they are confident this is not a replay of the giddy rise and precipitate decline of the Neuer Markt, the “growth” segment of the Frankfurt exchange that was disbanded in 2003 after the bursting of the technology bubble and a run of scandals. Today's companies are of better quality, they say, and are trading at price/earnings ratios of under 30, which is dear but not daft.

A hunger for new issues helps. There has been only a trickle of IPOs since 2000, the year the bubble burst, when there were 153. In 2005 there may be 20 in all; in 2006, perhaps double that. The strength of the German stockmarket has been a boon too. The main indices have risen steadily over the past 12 months, and even shrugged off last month's inconclusive general election. The DAX index of the 30 top companies is up by 30%, the MDAX of medium-sized firms by 40% and the small-cap SDAX by 50%. All this is encouraging brokers to push for an “alternative standard” market for smaller firms, perhaps before the end of the year, as a rival to London's AIM.

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Economist.com FINANCE & ECONOMICS

Europe's small-cap stockmarkets

A bigger pool for minnows

Oct 6th 2005
From The Economist print edition

New calls for a pan-European exchange to boost small and mid-sized companies

SHARE a latte with Europe's high-tech entrepreneurs and you'll quickly learn that most dream of selling out to Microsoft or another American giant. It makes sense, they say, because an initial public offering (IPO) in Europe is not realistic for most small firms. Unlike America, Europe has fragmented stockmarkets that lack the liquidity (and good equity research) to make many small-cap listings worthwhile.

Now financiers are declaring that it is high time a pan-European small-cap market was set up to funnel capital to corporate minnows. The European Private Equity & Venture Capital Association (EVCA) has issued a report saying that venture capitalists, executives at growth companies (especially high-tech firms), bankers and institutional shareholders would benefit.

European disunion

IPOs on Europe's stock exchanges, first half 2005

Exchange	Number	Value,€ bn
London	172	7.5
of which AIM	*152*	*2.1*
Euronext*	22	2.4
Oslo	19	0.5
Warsaw	18	0.7
Luxembourg	12	1.2
Frankfurt	6	1.9
Milan	5	1.2
Vienna	4	1.1
Zurich	4	0.4

*Owns Amsterdam, Brussels, Lisbon and Paris exchanges

Source: PricewaterhouseCoopers

A separate report this week by Oxford Analytica, a research firm, on behalf of the London Stock Exchange (LSE) says that such an exchange could increase GDP in the European Union by 0.3% to 0.6%. The LSE will be pleased by the conclusion that its own Alternative Investment Market (AIM), Europe's most active small-cap market (see table), is best suited to the role.

AIM immediately unveiled a plan to invade the continent with a network of nominated advisers ("nomads" bring companies to market) and to develop new investors. Chris Gibson-Smith, the LSE's chairman, told a risk-capital conference that up to 5% of mid-sized firms in Poland, Hungary and the Czech Republic could go public in the next five to ten years.

The idea of a pan-European exchange for small firms is not new. EASDAQ, since acquired by America's NASDAQ, tried and failed. Germany's defunct Neuer Markt also had continental aims before it imploded (see article). “The problem has been nationalism,” says Michael Elias, head of the EVCA's high-tech committee. He criticised Euronext's launch last year of Alternext, a market geared to smallish firms, for increasing fragmentation. Now OMX, the Nordic exchange operator, says it plans a small-cap market.

The EVCA lists a lot of things that would help a pan-European exchange to succeed: harmonisation of listing criteria, aggressive marketing, easy connectivity for investment banks from remote locations and low-cost settlement. It also wants barriers to cross-border capital flows to be removed and to see more independent research on small firms.

But even this might not be enough. Small European companies choose not to list on exchanges for many reasons. Many simply think they are too small. Others say that flotation is not relevant to their businesses, is too time-consuming, brings stringent listing and other criteria, costs too much or would dilute their equity. They have not been won over yet.

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Economist.com FINANCE & ECONOMICS

Economics focus

Be my guest

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The economic case for temporary migration is compelling; the historical record less so

LABOUR is globalisation's missing link. The flow of workers across borders is heavily impeded, leaving the global market for labour far more distorted than those for capital and commodities. The world price of capital may be set in America, and that of oil set in Saudi Arabia. But there is no such thing as a world price of labour. Wages can differ by a factor of ten or more depending only on the passport of the wage-earner, according to Dani Rodrik, an economist at Harvard.

Relaxing the movement of labour even a little would thus generate large efficiency gains. Mr Rodrik calculates that letting poor workers into rich countries, in modest numbers (equivalent to 3% of the hosts' labour force) for a limited period, could reap benefits to the developing world worth $200 billion a year. With numbers like that, he and other economists wonder why so much energy is spent freeing trade and capital, and so little expended freeing labour.

As if in answer to that rebuke, Kofi Annan, the secretary-general of the United Nations, set up the Global Commission on International Migration almost two years ago. The commission, 19 members of the great and good from around the world plus a secretariat in Geneva, was charged with inspiring debate and reflection on all aspects of international migration and policy. On October 5th, it published its report.

Of its 33 recommendations, the most consequential is indeed a call for more temporary migration from poor countries to rich ones. Guest-worker programmes would realise some of the efficiency gains identified by Mr Rodrik. Opening up new avenues of legal migration might also help reduce the flow of illegal migrants, the report hopes.

As the commission acknowledges, history lends little support to their optimism. The *Gastarbeiter* programme in Germany—which invited Turks, Yugoslavs and others needed at the time to fill the factory jobs created by the country's post-war economic miracle—failed, at least on its own terms. Many of Germany's “guests” never left, and their families soon arrived. The *bracero* programme in America—which, from 1942 to 1964, recruited Mexican field hands to pick cotton and sugar beets in Texas and California—fared no better. The entry of hundreds of thousands of farm workers provided camouflage for a substantial flow of undocumented labour.

Nonetheless, the logic of temporary migration appears irresistible. Rich countries want migrants' labour, but do not want to look after these newcomers when they grow old. Ideally, rich countries would like a constant rotation of workers, arriving while they are young and active, leaving before they grow old and dependent. For its part, the commission argues that “temporary and circular migration” is also better for poor countries. One reason is remittances: the longer an immigrant stays away from home, the smaller the share of his wages he sends back.

If temporary worker programmes make a comeback, how should they be designed? In a paper written for the commission, Martin Ruhs, of Oxford University, explores the options. Some

countries set a simple quota, filled on a first-come, first-served basis. The British government is more calculating, allocating visas to specific sectors, such as food processing, that express a need for cheap labour. Singapore is the most ambitious. Its ministry of manpower sets “foreign worker levies” that employers must pay to hire an immigrant. The levies differ by industry and by skill. To hire a skilled foreigner in construction, for example, an employer must pay S$80 ($47) a month. To hire an unskilled migrant, the employer must pay S$470. With these levies, the ministry can fine-tune the demand for immigrant labour.

Governments often claim they want to tailor rules on immigration to the needs of the economy. But the economy's needs also adapt to those rules. Philip Martin, of the University of California, Davis, and Michael Teitelbaum, of the Alfred Sloan Foundation, provide two striking examples. California's ketchup industry relied heavily on Mexican *braceros* to pick its tomatoes in the 1960s. The industry insisted it could not survive without these cheap hands. But when the *bracero* scheme was ended in 1964, farmers replaced the migrants with machines. Engineers invented a harvester that could shake tomatoes from plants and distinguish red fruit from green. Crop scientists developed new, ovoid tomatoes that the machines found easier to handle.

In Germany, Mr Martin and Mr Teitelbaum argue, the same phenomenon happened in reverse. The availability of cheap guest-workers in German factories slowed the adoption of new labour-saving technology. As the saying went at the time: Japan is getting robots while Germany gets Turks.

Some economists argue that governments should simply set a quota of visas and auction them. Alternatively, they could set a price for the permits designed to achieve more or less the same number of sales. The principal virtue of both schemes is that they allocate visas according to private perceptions of their worth, not government guesses about need.

Auf Wiedersehen, pet

How can governments ensure that guest workers do not overstay their welcome? In South Korea, temporary workers contribute to a special account that is refunded to them if they leave on time and forfeited if they linger. The British government is thinking of asking some migrants to post a bond, like a defendant on bail, which they will lose if they choose not to return.

If the economic gains to migration were not so great, the huddled masses would not be so reluctant to leave the rich world when they get there. “There is nothing more permanent than temporary migration,” cynics always say. But equally persistent are the market forces and demographic pressures that make temporary migration worth considering anew.

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Economist.com SCIENCE & TECHNOLOGY

The Nobel prizes

Fame, at last

Oct 6th 2005
From The Economist print edition

Prizes for the elimination of stomach ulcers, an explanation of light, a better clock and a better way of making chemicals

IT IS one of the paradoxes of the Nobel prizes—at least of those awarded for science—that while everyone agrees they are terribly important, usually no one has heard of either the winners or what they have done. For this year's medicine prize, though, that is only half true. It is, to be sure, unlikely that many readers will be familiar with the names of Barry Marshall and Robin Warren. But quite a few will be aware of their discovery. For Dr Marshall and Dr Warren are responsible for abolishing what was once one of the most frequent and unpleasant pieces of abdominal surgery: the cutting out of stomach and duodenal ulcers.

As the Karolinska Institute, the Swedish medical-research university that decides who gets the prize for medicine, realised, “their discovery of the bacterium *Helicobacter pylori* and its role in gastritis and peptic ulcer disease” was one of the most important medical findings of the 20th century. Until the two winners identified the bug responsible and showed what it was doing (in Dr Marshall's case by deliberately infecting himself), ulcers were seen as the result of a biochemical error (the production of too much stomach acid), often brought on by stress. In some circles, indeed, an ulcer was the badge of a hard-working executive: perhaps not as definitive proof of dedication to the job as a heart attack, but a lot less lethal. Now they are treated with antibiotics and a drug that reduces stomach-acid production.

The work of Dr Marshall and Dr Warren has certainly had an effect on everyday life. But if the Karolinska could be seen as playing to the gallery in giving them a prize, such an accusation could not be levelled at Sweden's Royal Academy of Science, which awards the physics and chemistry prizes. This year's winners could hardly be geekier. The academy gave half the physics prize to

Roy Glauber “for his contribution to the quantum theory of optical coherence”. The other half, divided evenly, went to John Hall and Theodore Hänsch “for their contributions to the development of laser-based precision spectroscopy, including the optical frequency comb technique”. Meanwhile the chemistry prize, also split three ways, was awarded for “the development of the metathesis method in organic synthesis”. In this case Yves Chauvin, Robert Grubbs and Richard Schrock were the recipients.

Fiat lux

Dr Glauber's contribution to science, translated into English, was to drag the field of optics into the modern, quantum world. Quantum theory started at the beginning of the 20th century, in part with work on light. But it was, ironically, not until the invention of the laser in 1960 that understanding the quantum nature of optics became crucial. Before then, although physicists knew that light was a quantum phenomenon, they had been able to get away with using the old wave-based descriptions. Afterwards, they needed a proper quantum theory, and Dr Glauber provided it. If the length of time this took is ironic, however, the 40-plus years that elapsed before the achievement was acknowledged are even more so.

Dr Hall and Dr Hänsch, meanwhile, are responsible for taking the art of measurement to new extremes. An optical frequency comb is a way of measuring the frequency of light with great precision. That, in turn, can be used to measure time in segments a few billionths of a billionth of a second long, and distance with similar accuracy—which might seem pointless, but is vital when studying such things as the speed of the chemical reactions for which the chemistry prize was awarded.

Metathesis, the technique for which Dr Chauvin, Dr Grubbs and Dr Schrock will receive their prizes, is a form of chemical sleight of hand that allows groups of atoms to be moved efficiently from one molecule to another. Dr Chauvin worked out the theory in the early 1970s, while in the 1990s Dr Grubbs and Dr Schrock used that theory to design catalysts that make the process far more effective. Since the molecules involved (so-called organic molecules, which are organised around a core of interconnected carbon atoms) are the basis of industries as diverse as petrochemicals and drugs, this technique has had as great a practical impact in its area as the discovery of *H. pylori* has had on medicine. Not all that is famous is important, and not all that is important is famous.

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Economist.com SCIENCE & TECHNOLOGY

Influenza

Unhappy rebirthday

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From The Economist print edition

Scientists have recreated the 1918 flu virus in order to reveal its secrets

THE winter of 1918 was particularly harsh because a pandemic of influenza was swirling around the globe. That November it felled an Alaskan woman whose body was interred in the frozen ground. Now, using samples taken from her lungs, and from autopsies of others among the estimated 50m people killed by influenza that year, the genetic sequence of her slayer has been identified. This sequence has allowed researchers to reconstruct a simulacrum of the 1918 virus. Since August of this year, the reborn virus has been held in controlled conditions at the Centres for Disease Control and Prevention (CDC) in Atlanta, Georgia.

This week *Nature* published the last part of the virus's genetic sequence, completing a decade-long effort by Jeffery Taubenberger and his team of scientists at the Armed Forces Institute in Maryland. The reconstruction of the live virus, announced simultaneously in *Science*, was done by Terrence Tumpey at the CDC and a group of researchers at the Mount Sinai School of Medicine in New York. The sequenced bits of the virus were spliced together and transferred into bacteria. The bacteria were then inserted into cultured cells and the viral genetic material reorganised itself to form a real virus.

The 1918 virus was very different from the viruses that caused more recent pandemics in 1957 and 1968. In those latter years, normal human influenza viruses became particularly virulent because they acquired two or three extra genes from an avian influenza strain. In 1918, it seems that the virus was entirely avian in origin. In other words, a bird-flu virus crossed to humans and adapted to them.

Dr Tumpey's team went on to create many genetic variants of the 1918 virus, in which they replaced its genes with their equivalents from more ordinary flu strains. This allowed them to identify which genes were responsible for making the 1918 virus so virulent, as each new variant was tested on mice, chicken embryos and human lung cells. In the 1918 virus, for example, a particular version of the gene that encodes a protein called haemagglutinin, which is found in the virus's outer coating, was essential for the development of severe pulmonary disease.

Work on the genetics of influenza is important for many reasons. Studying the links between genetic changes and changes in the way the virus behaves is likely to help in the process of choosing effective countermeasures against emerging strains and in finding ways of designing better vaccines. The research might even lead to the development of antiviral drugs that work by interfering with the genes responsible for producing virulence in pandemic viruses.

Another intriguing possibility raised by Dr Taubenberger's team is that avian viruses may adapt to humans in a predictable sequence. It seems likely that only a small number of genetic changes were required to turn bird flu into the 1918 pandemic. And it turns out that such genetic changes are also found in other human-pathogenic strains of avian viruses, such as H7N7 and H5N1.

If these mutations are what allow the avian virus to replicate more easily in human cells, then it

might be possible to generate a genetic “check list” of dangerous-looking mutations that would allow virus surveillance to be far better focused than it is today. Indeed, H5N1 is already picking up the kinds of mutations that made the 1918 virus dangerous. The researchers think it possible that forces similar to those at work in 1918 are driving H5N1 down a similar evolutionary path. Every time the virus infects a human, or even another mammal such as a pig or a dog, viral replication will generate further genetic changes and some of these will make the virus better at breeding in people. The one bit of good news is that it does not appear that H5N1 is very far along this path yet. The relevant mutations are still scattered among different strains. Some comfort then, but not much.

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Fuel efficiency

A dose of Clap

Oct 6th 2005
From The Economist print edition

Putting dust in your engine sounds crazy. But it might not be

ALTHOUGH they need to fire their brand consultants, the inventors of Clap—an additive intended to improve the fuel-efficiency of car engines—seem to be on to something. By pulverising a mineral called serpentine into particles a millionth of a millimetre in diameter, they have come up with an additive which, they claim, can improve the fuel consumption of old car engines by as much as 10%. And, a millionth of a metre being a nanometre, they are also claiming that their product is an example of that much talked of, but little-seen field known as nanotechnology.

The Clap project began in 1979 at the presciently named Institute of Nanotechnology in Moscow. The idea was to produce not a fuel additive, but a lubricant additive. The institute's engineers, led by Fiodor Wischnjewsky, thought that adding a suitably fine powder to an old engine's oil would effect continuous running repairs by filling in tiny cracks and abrasions in the cylinders and pistons. These irregularities make combustion inefficient, which increases both fuel consumption and pollution.

This being first the Soviet Union and then Russia, nothing much happened until 2002 when Francesco Meneguzzo, an engineer at the Biometeorology Laboratory in Florence, got wind of the project. Then things started moving.

The Italians ditched the Russians' efforts to design copper, zinc, aluminium and silver nanopowders. These rendered the oil too fluid. Instead, they concentrated on serpentine, a substance rich in magnesium silicate which was found to cling efficiently to the internal surfaces of all common petrol and diesel engines.

The problem was how to crush this mineral into small enough particles on an industrial scale. Industrial grinding mills made of hardened steel cannot be used since they release heavy metals into the milled rock, replicating the problems of metallic nanopowders. To overcome this, the engineers came up with a two-stage process, the first stage of which goes back to the origins of grinding mills by employing actual millstones made of granite. The second stage is ultramodern, though. The particles of mineral-flour made by the millstones are blown into nanosmithereens by tiny electrical charges.

The result, which requires a half-gram dose to be squirted into a car's oil every 40,000km, will go on sale in December. Old cars may soon, therefore, be clapped out in more senses than one.

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Economist.com SCIENCE & TECHNOLOGY

Cosmology

A braney theory

Oct 6th 2005
From The Economist print edition

An explanation for the anthropic principle comes a little closer

DID God have a choice? Or, to put the matter less theologically, does the universe have to be the way that it is? The answer to this question, posed by Einstein among others, remains elusive. But it is important, not least because a universe with laws only slightly different from those actually observed would be one in which life—and therefore human life—could never have come into existence.

That observation, known as the anthropic principle, disturbs many physicists because they cannot see any fundamental reason why things could not be different. In particular, they cannot see why space has to have three dimensions. But a paper due to be published this month in *Physical Review Letters* by Andreas Karch of the University of Washington and Lisa Randall of Harvard University suggests that the laws of physics may, indeed, be biased towards three-dimensions. Curiously, though, they have a similar bias towards seven-dimensions.

The idea that there may be more dimensions than the familiar ones of length, breadth and height (and also, to be strictly accurate, the fourth dimension of time) is a consequence of attempts to solve an old problem in physics. Ever since Einstein developed his theories of space, time and gravity, physicists have sought a “theory of everything” that would unite those theories with quantum mechanics—the part of physics that describes electromagnetism and the forces that hold atomic nuclei together. Such a theory would, it is hoped, describe how the universe developed from the Big Bang. It would explain why there appears to be more matter than anti-matter. It would even indicate the nature of the dark energy and dark matter that lurk at the edge of perception.

To date, the best candidates for a theory of everything are various versions of a branch of mathematics called string theory. Unfortunately for common sense, these theories require the universe to have ten or even 11 dimensions rather than the familiar three of space and one of time. To get round this anomaly, some physicists propose that the familiar dimensions are “unfurled”, while the other six or seven are rolled up so tightly that they cannot be seen, even with the most powerful instruments available. For an everyday analogy, think of a thread of cotton. This appears one-dimensional for most purposes. Only under a magnifying glass are the other two dimensions perceptible.

A second interpretation of multidimensionality, however, is that the extra dimensions are not always rolled up, but that even when they are not humans cannot readily observe them because they are not free to move in them. In this version, the space inhabited by humans is a three-dimensional “surface” embedded in a higher dimensional landscape. The particles of which people are composed, and the non-gravitational forces acting on them, are strictly confined to this surface—called a brane (short for membrane)—and, as such, have no direct knowledge of the higher dimensional space around them. Only gravity is free to pervade all parts of the universe, which is one of the reasons why it obeys a different set of rules from the other forces.

It is this second interpretation that is invoked by Dr Karch and Dr Randall. They assume that, initially, the universe was filled with equal numbers of branes and anti-branes (the antimatter equivalent of a brane). These branes and anti-branes could take any number of up to ten different dimensions. Dr Karch and Dr Randall then demonstrated, mathematically, that a universe filled with equal numbers of branes and anti-branes will naturally come to be dominated by 3-branes and 7-branes because these are the least likely to run into their anti-brane counterparts and thus be annihilated.

This result is interesting for two reasons. It is the first piece of work to show that branes alone can explain the existence of hidden dimensions. They do not have to be rolled up to be inaccessible. It is also the first to suggest an underlying preference in the laws of physics for certain sorts of universe, and thus perhaps provide a solution to the anthropic principle. Yet it is not a total solution. Other realities, whether three- or seven-dimensional, could be hidden elsewhere in the landscape. And life in seven-dimensional space would look very different from life on Earth—if, indeed, it existed at all. That is because the force of gravity would diminish far more quickly with distance than it does in this world. As a result, seven-dimensional space could not have planets in stable orbits around stars. Like dark matter and dark energy, therefore, the anthropic principle is still grinning from the sidelines, taunting physicists to explain it.

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Racing rockets

Oct 6th 2005
From The Economist print edition

AFP

As Alfred Nobel knew, prizes spur innovation. That fact, more than any other, has been taken to heart by Peter Diamandis, the space enthusiast who invented the Ansari X-Prize in order to encourage entrepreneurs to design and build new kinds of spaceship. Almost a year ago, *SpaceShipOne* received the $10m prize for making it into space twice in a fortnight, and today a commercial version of this ship is being built. But Mr Diamandis is not happy to rest on his laurels. He has now turned his attention to another pressing requirement of the space industry: better propulsion. So this week he launched his latest wheeze: the Rocket Racing League—Formula 1 racing in the skies. The idea is simply to race rockets, at many hundreds of kilometres an hour, around a course. Exciting to watch, and almost certain to inspire innovation among those who compete. The first generation of racers are currently being built by XCOR Aerospace of Mojave, California—a company based in a hangar only steps away from where *SpaceShipTwo* is under development.

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Partisan political books from America

Fools' gold

Oct 6th 2005 | WASHINGTON, DC
From The Economist print edition

AP

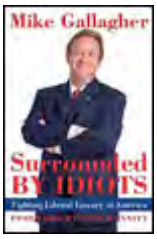
As America becomes more polarised, its political writing is getting worse

POLITICAL debate in America seems to grow less civil by the hour. Louisiana's senior senator recently threatened to punch the president. At marches against the Iraq war, the “Fuck Bush” placards outnumber those saying “Give peace a chance”. Even the mild, urbane new chief justice gets called “Neanderthal”. So it should come as no surprise that political books are becoming coarser and more crudely partisan—and that crud sells.

Looking at the array of titles published since 2000, it is easy to despair. There has been Clint Willis's “The I Hate George W. Bush Reader: Why Dubya is Wrong About Absolutely Everything”, which is not to be confused with “The Bush-Hater's Handbook: A Guide to the Most Appalling Presidency of the Past 100 Years” by Jack Huberman. On the other side we've seen “Why the Left Hates America” by Daniel Flynn and a series of books by Ann Coulter who labels liberals liars, traitors and fools.

If one takes the plunge and actually reads some of the more recent polemics, the urge to despair becomes all but irresistible. Take, for example, “Surrounded By Idiots: Fighting Liberal Lunacy in America” by Mike Gallagher. Mr Gallagher is a talk-radio host who, as you may have guessed, leans to the right. His political observations are not exactly profound. Michael Moore, he says, “is a nasty, ugly man”; John Kerry

Surrounded By Idiots: Fighting Liberal Lunacy in America
By Mike Gallagher



William Morrow; 240 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

Liberalism is a Mental Disorder:

routinely queue-barges at his local coffee shop. Moving from the particular to the general, Mr Gallagher explains that the left is trying to destroy "every value and standard, principle and ideal, concept of God, family, honour, duty, country and decency that we hold dear." He concedes, however, that he "cannot find a valid reason to blame liberals" for the fact that he used to be fat.

One finishes this book persuaded by Mr Gallagher's thesis: that he is surrounded by idiots. That would certainly explain why he was unable to do any research. But the book is not wholly without merit. It shines a useful light on the techniques of modern talk radio. Mr Gallagher is adept at stunts that mock his ideological opponents, or simply upset them.

For example, Al Sharpton, a lefty preacher, once vowed to sleep out in a cardboard box on a winter night to protest at the plight of the homeless. Mr Gallagher discovered that he had a reservation at a local hotel, after which he mounted a "Reverend Al Watch" in front of his box to make sure the preacher couldn't sneak into a warm hotel room as soon as the cameras had left. Another time, to annoy what he regarded as the all-too-earnest People for the Ethical Treatment of Animals, he broadcast the death of a steer, and then donated its meat to the homeless.

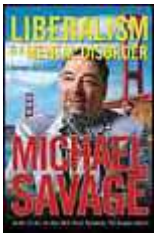
An altogether less agreeable polemicist is Michael Savage, whose latest book is called "Liberalism is a Mental Disorder". He calls homosexual activists "brown shorts" and thinks Mr Bush has messed up by not killing nearly enough people in Iraq. He believes that the United Nations and other shadowy international groups are planning to "over-ride our democracy" and replace the Bill of Rights with "a new, watered-down bill of wrongs from the new, ruling bureaucrats". He wonders why Republican leaders have not warned people about this. He uses the term "village idiots" to describe a body—the Democratic Leadership Council—whose name he cannot spell.

Bernard Goldberg, by contrast, is far too clever to have written a book like "100 People Who Are Screwing Up America", but he did and it is selling exceedingly well. A former CBS correspondent, Mr Goldberg first rose to prominence with a book exposing liberal bias on the television network news. Now he reveals that he dislikes all the prominent liberals in the country. Plus Mr Savage, who is beyond the pale even for his fellow right-wingers.

"The Vast Left Wing Conspiracy" by Byron York is, despite its title, quite sane. Indeed, it offers some subtle insights into why American politics are so polarised. Mr York, a correspondent for the conservative *National Review*, notes that since a new campaign-finance law imposed tight limits on how much anyone could give to a candidate or party, the biggest donors have put their millions into "independent" campaign groups, which they effectively control. This means that "eccentric billionaires" such as George Soros are able to dictate, more than ever before, the tone and message of political campaigns.

In a parallel development, given the low turnout at American elections, both parties think they have more to gain by rousing those who already support them to get to the polls, rather than by appealing to swing voters.

Savage Solutions
By Michael Savage



Nelson Current; 272 pages; $25.99

Buy it at
Amazon.com
Amazon.co.uk

100 People Who Are Screwing Up America (and Al Franken is #37)
By Bernard Goldberg

HarperCollins; 320 pages; $25.95 and £14.99

Buy it at
Amazon.com
Amazon.co.uk

The Vast Left Wing Conspiracy
By Byron York

Crown Forum; 288 pages; $26.95

Buy it at
Amazon.com
Amazon.co.uk

Dictionary of Republicanisms
By Compiled by Katrina vanden Heuvel

George Bush may have shown this week, by nominating his former personal lawyer to be the Supreme Court's ninth judge, that he has no appetite for bloody ideological battle, but on the whole politicians emphasise divisive issues—such as gay marriage or Iraq—to get their base angry enough to vote. Mr York's analysis of how this makes politics nuttier focuses solely on the left, but then he had to justify his title somehow.

For some reason, the Democrats have produced few notable polemics this year. Next month sees the publication of a “Dictionary of Republicanisms”, compiled by the editor of the *Nation* magazine, which shows the extent to which tribal affiliation now substitutes for wit. “Free markets”, for example, are defined as “Halliburton no-bid contracts at taxpayer expense”. Surely liberals can do better than this.

Does the profusion of mindlessly partisan books matter? One could argue that it depends on whether Mr Gallagher and his fellow writers are crowding out more nuanced works or complementing them. If their rants are being read by those who would otherwise read nothing, they may even increase the spread of knowledge.

It is hard, though, to sustain such a sanguine view. Sensible, scholarly political books still get published, but the market rewards the sort you can judge by the cover. Political writing is unhealthily partisan largely because that is how America is: the current and former presidents each have qualities that particularly enrage their opponents. But partisan writing surely aggravates the red-blue divide as well as merely reflecting it. Michael Barone, a conservative writer, says he finds it hard these days to find Democrats with whom he can have a sensible conversation. One should take Mr Barone's views on the mindless polarisation of political discourse with a grain of salt, however. His “Almanac of American Politics” is superb, and so balanced that it is used by both sides of the political divide. But then it doesn't sell nearly as well as the rubbish.

Surrounded By Idiots: Fighting Liberal Lunacy in America.
By Mike Gallagher.
William Morrow; 240 pages; $24.95

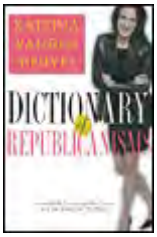
Liberalism is a Mental Disorder: Savage Solutions.
By Michael Savage.
Nelson Current; 272 pages; $25.99

100 People Who Are Screwing Up America (and Al Franken is #37).
By Bernard Goldberg.
HarperCollins; 320 pages; $25.95 and £14.99

The Vast Left Wing Conspiracy.
By Byron York.
Crown Forum; 288 pages; $26.95

Dictionary of Republicanisms.
Compiled by Katrina vanden Heuvel.
Nation Books; 224 pages; $14.95

The Almanac of American Politics, 2006.



Nation Books; 224 pages; $14.95

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The Almanac of American Politics, 2006
By Michael Barone, Richard E. Cohen and Grant Ujifusa

National Journal Group; 1907 pages; $69.95

Buy it at
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By Michael Barone with Richard E. Cohen and Grant Ujifusa.
National Journal Group; 1907 pages; $69.95

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Foreign policy and the courts

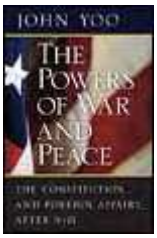
Backing off

Oct 6th 2005
From The Economist print edition

AP

Have you read the memos?

The Powers of War and Peace: The Constitution and Foreign Affairs After 9/11
By John Yoo



University of Chicago Press; 378 pages; $29

Buy it at
Amazon.com
Amazon.co.uk

ONE book that might well have been grossly partisan, but is not, is John Yoo's “The Powers of War and Peace”. Mr Yoo is one of America's most controversial lawyers. While serving in the Department of Justice from 2001 to 2003, he wrote or helped to write highly contentious legal opinions justifying the Bush administration's aggressive approach to detaining and interrogating suspected terrorists.

Mr Yoo argued that the Geneva Conventions did not apply to “enemy combatants” captured in Afghanistan or anywhere else in the administration's “war on terror”. He claimed that federal laws against torture banned only extreme pain equivalent to that “accompanying serious physical injury, such as organ failure, impairment of bodily function, or even death”. And he said that, in any case, the president, as commander-in-chief engaged in a war, is not subject to these laws, nor would anyone be who followed his orders.

When these memos were revealed in 2004, at the time that the torture at Abu Ghraib became public, there was an outcry. Mr Yoo has vigorously defended his stance and has recently recommended that the president order the assassination of suspected terrorists. Although the Bush administration has since distanced itself from many of Mr Yoo's views, he still remains a darling of right-wing legal circles.

Given his reputation and his taste for clear and provocative opinions, Mr Yoo could well have written an incendiary work on fraught issues of war and peace. The real surprise is that he has not. His book is well-written if dry, festooned with the usual footnotes, summarising long-running debates among constitutional scholars about the appropriate balance of power between the president and Congress in formulating foreign policy and making war.

Mr Yoo correctly observes that the constitution seems to strike a balance between executive and legislative branches in these areas, but it is somewhat vague about precisely what that balance is. He also correctly says that, in practice, things have not worked out strictly according to the constitutional text. Presidents often launch America into armed conflicts without formal declarations of war, and have sometimes not sought any kind of congressional authorisation, for example. Some scholars decry this, others don't. No one denies that this has been the case. Mr Yoo also correctly predicts that globalisation and the growth of multilateral treaties and institutions will make this situation even more complicated, and ambiguous.

All this is reasonable and mainstream. Mr Yoo writes clearly and calmly. He confuses the topic a little by first claiming that the original intention of the constitution's ratifiers cannot really be expected to resolve the ambiguous relationship between Congress and the president when it comes to foreign affairs. Then he argues, in what is supposed to be his own original contribution, that their intention was, in fact, that this relationship be ambiguous, or “dynamic” as he terms it.

Despite this contradiction, Mr Yoo's book is perfectly adequate, and his descriptions of the scholarly debate will interest a small coterie of constitutional specialists. But this is not what some of his conservative fans might have hoped for: a full-blooded defence of the view behind all those exciting Department of Justice memos in which he had a hand. In those memos, the president's powers in pursuing the war on terror are portrayed as literally unlimited, beyond the reach of Congress, federal or international law or any other constraint. For some reason Mr Yoo seems to have stepped back from that precipice (beyond which, many would argue, there is no rule of law). Instead, he wrings his hands, and declares how complicated everything is. How true.

The Powers of War and Peace: The Constitution and Foreign Affairs After 9/11.
By John Yoo.
University of Chicago Press; 378 pages; $29

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Economist.com BOOKS & ARTS

Fascism in Italy

The F word

Oct 6th 2005
From The Economist print edition

ACADEMIC studies of fascism have tended, in the past, to concentrate on its leadership or ideology. Only recently have scholars sought to look at the lives of ordinary people and analyse what happened to the grandiose slogans when they were translated into the currency of everyday living.

Three years ago, Richard Bosworth, an Australian historian, wrote what is perhaps the best biography of Mussolini in English. But he was challenged by one reviewer on whether biography could ever adequately explain the terrible events of inter-war Europe. “Mussolini's Italy” is his response: an attempt to outline the impact of fascism upon Italian society. It is a powerful work of scholarship, beautifully written, which should be read by anyone interested in 20th-century Europe, or indeed the antecedents of modern-day Italy.

Mussolini's Italy
By R.J.B. Bosworth

Penguin/Allen Lane; 692 pages; £25.

Buy it at
Amazon.co.uk

Mr Bosworth is concerned to destroy two myths. The first is the Captain Corelli fallacy, that says Italian fascism was something of a joke; such nice, bumbling, charming people as the Italians, *brava gente*, could never have done such horrible things. Mussolini, it is argued, was but a precursor of Silvio Berlusconi, and fascism merely an earlier form of Berlusconi's authoritarian paternalism. “Of all the nations in the world, it seems, Italians are the last to be typecast as willing executioners”. Mr Berlusconi has himself given some currency to the myth, declaring, in 2003, that Mussolini never killed anyone and that the anti-fascists pent up *in confino* were actually in a kind of “holiday camp”.

Mr Bosworth rightly has little truck with such apologias. For it was Italy which, between the wars, led the assault on the humanist ideals of the Enlightenment. Fascist Italy supplied a new model of government, improved upon by Hitler, so that Italy's own special version of racism bears some responsibility for “escorting the world to Auschwitz”. The regime, however, attacked not only Jews, but also Arabs, blacks and Slavs. One secretary of the Fascist Party went so far as to advocate the liquidation of all Slovenes. Mr Bosworth calculates that the regime was, through its European and colonial wars, responsible “for the premature death of a million people”. Sadly, some Italians have still not come to terms with the crimes committed during these years.

The second myth is that Italy was in reality what Mussolini claimed it to be, a totalitarian society. The originality of Mr Bosworth's thesis lies in his examination of what Italians were actually doing under the regime rather than what its leaders said that they were doing. “Fascism was an affair of the gut more than of the brain”, so any study which treats “only the thinkers and the writers misses the most powerful impulse of all.” Mr Bosworth shows that “Time and again, Italians proved able to give lip-service to totalitarianism while retaining a sense of self.” Italy does not fit the caricature of being led by a madman “who intruded his fundamentalism into every nook and cranny of his subjects' minds.” Although Mussolini did indeed seek to manipulate and control Italians, the people were at least equally skilful at adapting fascism to their own needs.

Fascism's achievements, both negative and positive, have been consistently exaggerated. It did not destroy Italian democracy; before 1922 Italy was only dubiously democratic. “Traces of what might be deemed a proto-fascism” can already be detected in the preceding, Liberal, regime. Nor did fascism succeed in transforming a society with powerful and complex ties of patronage and loyalty—to the monarchy, the church, and, above all, the family—“whose cast was as frequently local as it was Italian, let alone fascist”. Too many generalisations about Italian society reflect the ideology, even the mythology, of fascism, rather than its realities.

In the end, all the promises of fascism turned out to be false, so that Italians were wise to remain “more suspicious than believing”. By 1945, they could find “solace in the understanding that, under a dictatorship such as Benito Mussolini's, to endure was all.” The impermeability and lack of plasticity of human nature provide a rare message of hope in this otherwise dismal story of a wicked dictatorship.

Mussolini's Italy.
By R.J.B. Bosworth.
Penguin/Allen Lane; 692 pages; £25.
To be published in America by Penguin Press in February

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Lessons of seduction

Picking up pieces

Oct 6th 2005
From The Economist print edition

NEIL STRAUSS'S college years were wretchedly chaste. Even when he landed a job as a rock reporter with the *New York Times*, the closest he got to unfettered hedonism was a peck on the cheek from Tommy Lee. “Some guys had it”, Mr Strauss remembers. “Other guys didn't. I clearly didn't.”

Then Mr Strauss discovered the online world of Pickup Artists (PUAs), a vast internet community where self-styled seduction gurus with names like Mystery and Juggler dispense their techniques to grateful acolytes in virtual lounges and locker-rooms. Wryly admitting his AFC status (average frustrated chump), Mr Strauss logs on as Style, achieves PUA stardom and becomes role model and tutor to a new generation of AFCs. This is the game.

The world he enters is hermetically masculine, and as loaded with jargon as a Pentagon laptop. Hunting for women is “sarging”, and is often carried out with a “wingman” in attendance. If “cockblocked”, you can deploy a “boyfriend-destroyer pattern”. Go in under the radar, Mystery counsels Mr Strauss, rather than approaching a target with a sexual come-on. “Learn about her first, and let her earn the right to be hit on.”

The Game: Penetrating the Secret Society of Pickup Artists
By Neil Strauss

Regan Books; 452 pages; $29.95.
Canongate; £16.99

Buy it at
Amazon.com
Amazon.co.uk

It's not long before the game dominates Mr Strauss's life. With his camouflage “openers” and his sniper “negs”—off-the-cuff deprecatory remarks intended to dent a woman's self-esteem—he is soon “closing” on a nightly basis. Returning briefly to his journalistic persona to interview Britney Spears, he finds himself gaming her, and she gives him her phone number.

The game giveth, but it also taketh away, as the author is all too aware. As reality blurs, Mr Strauss finds it increasingly hard to view women as anything other than targets on which to hone his technique. “We may have been supermen in the club”, he muses, “but on the inside we were rotting.” Redemption comes in the form of Lisa, who cares not a fig for Mr Strauss's patter. Lisa loves him, it turns out, for himself.

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Economist.com BOOKS & ARTS

Contract bridge

Grand slam

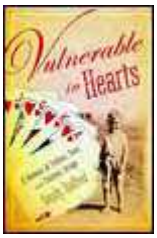
Oct 6th 2005
From The Economist print edition

JUST as Sandy Balfour's earlier memoir about crossword puzzles, “Pretty Girl in Crimson Rose (8)”, was not really about crossword puzzles, so his book about bridge is not really about bridge. The author's abiding interest is people smitten by a pastime. In “Vulnerable in Hearts” the cards take a distant second place to the card players and especially to the author's exasperating father, Tom. The old man was born in the 1920s, the decade when contract bridge was invented by Harold Vanderbilt, the scion of a fabulously rich shipping family.

Tom Balfour's life pretty much spanned the history of a once enormously popular game which, on the findings of social-connectedness surveys in the United States, now seems doomed to extinction. Sandy Balfour fears the decline goes far beyond America. By the time his Scottish-born father died in the summer of 2003 in South Africa, the Balfours' adopted land, the bridge evening was “an almost obsolete event” there too.

Even in suburban homes the once-famous names of bridge gurus celebrated in this book are now almost forgotten: strategists such as Charles Goren, the inventor of a system known as Standard American, and “Skid” Simon, a creator of the Acol system, who famously taught his adherents to aim for “the best result possible, not the best possible result” and to avoid fancy bids or plays their partners could not comprehend.

Vulnerable in Hearts: A Memoir of Fathers, Sons and Contract Bridge
By Sandy Balfour



To be published in America by Farrar, Straus and Giroux in April
Atlantic Books; 291 pages; £14.99.

Buy it at
Amazon.com
Amazon.co.uk

The one blessing to flow from the demise of bridge is that future generations will be spared a partner like Tom Balfour. He never learnt that communication is the essence of a game in which there are, on his son's reckoning, 635 billion possible individual hands and 53 octillion possible full deals. Instead of trying to empathise with his partner's bids and tactics, Tom took charge. “In Dad's mind the pursuit of points was nothing compared to the pursuit of glory.” When in doubt, his motto was to bid one more. In consequence, he lost in style, or at least comprehensively.

In the menagerie of bridge, as his son reluctantly admits, Tom Balfour belonged to the species known as Hideous Hog. The HH is insufferably arrogant. He wants to play the hand no matter what the cost and convinces himself that it is in his partner's interest that he does so. Tom's weaknesses were revealing. As his son is so sadly aware, whatever defects a person possesses will be worse at the bridge table. “Every chink in your character will be exposed and magnified.”

Tom's character was dramatically flawed. At the age of 13, he was plucked out of a happy home in Edinburgh and sent to South Africa to escape the war. He never really recovered from the shock of his sudden enforced exile and, as this poignant book suggests rather than spells out, in later life his consequent addiction to drink lost him his faith, dignity and self-respect. But he remained lovable to his son to the last—even when his reckless bids cost them rubber after rubber.

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By Sandy Balfour.
Atlantic Books; 291 pages; £14.99.
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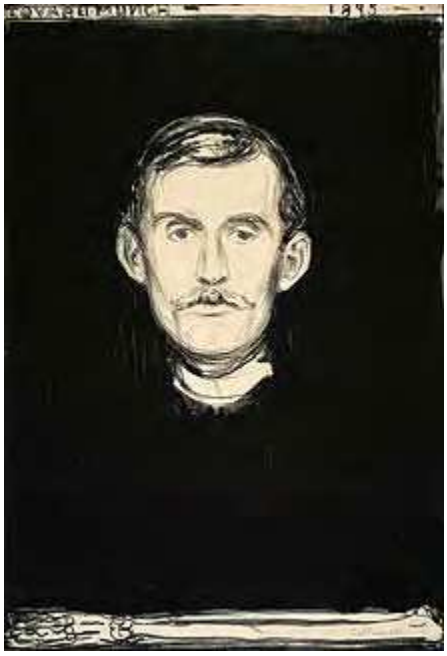
Economist.com BOOKS & ARTS

Edvard Munch

Dark lord

Oct 6th 2005
From The Economist print edition

The artist through his own eyes



Bonjour tristesse

EDVARD MUNCH may be just too familiar for his own good. Are you looking for an off-the-peg image of alienation? Reach for "The Scream". Searching for that archetypal image of the sulky, *fin-de-siècle* symbolist temptress? Pick Munch's "Madonna".

Munch may be on many a teenager's bedroom wall, but there is much that we don't know about Norway's greatest cultural export. Which is why a new show at London's Royal Academy of Arts is such a revelation. Munch was an obsessive self-portraitist. From teenage years to deathbed he made and re-made his own image with a feverish intensity. And his portraits offer a clear view of how he saw himself engaging with the world. When Munch felt persecuted, he depicted himself as burning in the flames of hell; when he was more composed, he flung out his arms, and sunlight appeared to flood across his skin.

Rembrandt, another obsessive self-portraitist, may have changed costume again and again, but beneath the cloth lay a man whose essential appearance changed relatively little because he maintained, from first to last, an unerringly stable sense of himself. By contrast, Munch's hold on what it meant to be Edvard Munch was far less sure. In this he is unlike any other great self-portraitist. No painter changes quite so much as Munch changes. No other self-portraitist has such a slippery sense of what he believes to be the essence of himself.

The first portraits belong to the teenage years. They are easily the most assured—almost cocky in their self-confidence. The image looks secure, bourgeois, somewhat haughty. The manner of self-portrayal leans towards the academic. The painted surface is relatively dense, and the paint evenly worked. Yet within a decade all that has changed. As Munch ages, the painted surface thins and thins, the strokes from his brush become more febrile, the colours are bolder, stranger and more unpredictably intense. Munch, by turns, looks ghostly, phantasmal, haunted.

"Edvard Munch: Behind the Scream", Sue Prideaux's new biography from Yale University Press, presents detailed evidence of the morbidity, instability and mental turmoil that so coloured Munch's inner landscape. The family had a history of insanity; his father was oppressively, brow-beatingly religious. As Munch himself once wrote, "Illness, insanity and death were the black angels that hovered over my cradle." For many years, Munch lived a nomadic and disorganised life, wandering across Europe. He was unloved and misunderstood in Norway. Germany was the first country wholeheartedly to appreciate his work. He finally returned to Norway in 1909, but until his death in 1944, he had an uneasy relationship with his native land.

Painting offered some means of escape. It enabled him to face down his demons and become reconciled with himself. Munch's paintings were his closest friends. He surrounded himself with them and hated to sell them. The kinds of paintings that he made represent a dissection of the human soul—his own in particular. For Munch, to paint realistically would have been to see the world as he never saw it.

“Edvard Munch by Himself” is at the Royal Academy of Arts, London, until December 11th

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Economist.com PEOPLE

August Wilson

Oct 6th 2005
From The Economist print edition

August Wilson, African-American playwright, died on October 2nd, aged 60

AP

IF EVER someone, following current fashion, decides to stage all the plays of August Wilson's epic cycle in a single session, the audience is in for a treat—and an endurance test. The cycle consists of ten plays, each set in a different decade of the 20th century. Long before the series was complete—“Radio Golf”, the last piece to be written, was finished only this year—Mr Wilson had been hailed as one of America's greatest playwrights, in a pantheon with such masters as Arthur Miller, Eugene O'Neill and Tennessee Williams.

It is too soon to say whether Mr Wilson will in the end hold his own against such talents, or whether he will be remembered chiefly as a superb dramatist of the collective black-American experience of the 20th century. That would be no small achievement, but it would probably be seen by Mr Wilson as a mark of failure. He believed that, though the world he portrayed was indeed the world of black America, or rather the much smaller world of the Hill district of Pittsburgh in which he grew up, nonetheless his plays dealt with the universal themes of beauty, love, honour, betrayal and so on.

He wrote about the characters he knew: ordinary people, not swells or celebrities, with ordinary people's imperfections. Perhaps, since these people were the descendants of slaves and continued to experience indignities long after slavery ended, they suffered more than other people, or at least differently from them. He certainly thought that only a black director was suitable for the film version of his play “Fences”, arguing that the task demanded someone who knew first-hand the culture of black Americans. The film came to naught but, no matter, lots of people saw the play. It ran for 525 performances on Broadway, made pots of money and won him a Pulitzer prize and a Tony award.

Tarnished city on the Hill

Such honours cascaded down on Mr Wilson but did not seem to turn his head or quench the anger that smouldered somewhere below the external affability. Some of that anger may have been in the genes: his father, an immigrant baker of German extraction who played little part in his children's upbringing, was said to have a quick temper. Young August got his values, though, especially his pride in African-American culture, from his mother, a cleaner. When she divorced her husband, the family moved to the suburbs and the boy was sent to a Catholic school, where he was the only black child in the class. There, as he was later to tell the *New Yorker*, he would find a note on his desk every day bearing the words, “Go home, nigger”. In a way, he did. He dropped out.

The local library then became his seat of learning, along with the shops, streets and bars of the Hill district, and the workplaces whose little incidents punctuated the boredom of a series of dead-end jobs. He thought his heart was in poetry, but discovered, on moving to St Paul, Minnesota, where he got a job at a museum turning Native American stories into children's plays, that drama was his métier.

Soon “Jitney” was written, a play set in 1977 in the seedy office of a taxi company where the drivers hang around on old sofas and Marvin Gaye plays on the radio. “Jitney” never made it to Broadway, though all but one of the other nine did and, years later, it was a sell-out at the National Theatre in London. By 1984, however, “Ma Rainey's Black Bottom”, the only one of the ten plays to stray away from Pittsburgh, had been put on at the Yale Repertory Theatre and then Broadway. Set in a Chicago recording studio in 1927, it explores the fraught relations among the members of the great blues singer's band and her white producer and agent.

These and the other plays were not at first conceived as a decade-by-decade series, nor were they written in matching sequence. But the themes recur and overlap, and some of the characters are linked. None is overtly political, though politics is never far beneath the surface. All are written in the social-realist style, and all are marked by Mr Wilson's gift for dialogue, his feeling for language and his capacity to evoke unsentimental emotion. They are also remarkably even in quality.

The plays have their critics. Many complain that they are repetitive. Some dislike the myth and mysticism that periodically creep in, as with Aunt Ester, a 287-year-old character who is referred to in several pieces and eventually appears in “Gem of the Ocean”, first staged in 2003. Others find the works didactic, or written in a confused variety of styles. In general, though, the fans vastly outnumber the detractors, at least when they see the Broadway productions. Had they seen earlier versions they might have been more critical: the plays have often been cut and changed before reaching New York. And it is clear that Mr Wilson always owed a large debt to Lloyd Richards, who directed “Ma Rainey” at Yale and on Broadway, and five of the other Broadway productions, pruning and sharpening them along the way.

If there is a single theme that runs through Mr Wilson's plays, it is the corrosiveness of the legacy of slavery, and the racism associated with it. That may be too limited a subject to lift Mr Wilson to the very top rank of playwrights. But it is surely big enough to keep audiences engrossed and admiring for years to come.

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Overview

Oct 6th 2005
From The Economist print edition

America's services sector may have been hurt by Hurricane Katrina, but the storm helped manufacturing in September. The Institute for Supply Management's services index fell sharply to 53.3 from 65.0 in August. However, the index of factory output climbed to 59.4, from 53.6 in the previous month, lifted by the demands of reconstruction along America's Gulf coast.

Consumer prices in the **euro area** rose by 0.5% in September, leaving them 2.5% higher than a year ago, according to preliminary estimates. Retail sales were stronger than expected, rising by 0.9% in August, after declining by 0.5% in July. The purchasing managers' index for manufacturing moved up to 51.7 in September from 50.4 in August. The services index also beat forecasts, rising to a 14-month high of 54.7. However, the unemployment rate worsened in August to 8.6%, from 8.5% in July.

Japan's Tankan survey of business confidence indicated more optimism in September, but fell short of expectations. The index for large manufacturers rose by only one point, to 19.0. Household spending, after recent declines, increased by 3.2% in August. The unemployment rate also improved to 4.3% in August, from 4.4% a month earlier.

Manufacturing expanded in **Britain**. The purchasing managers' index for manufacturing rose to 51.5 in September from 50.3 in August, beating expectations of a contraction.

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Output, demand and jobs

Oct 6th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q2	+ 5.2	+ 2.6	+ 3.3	+ 0.7	Q2	+ 1.6	Q2	5.0	Aug	5.7
Austria	+ 2.0	Q1	+ 0.8	+ 1.8	+ 2.0	+ 5.4	Jul	+ 1.7	Jun	5.2	Sep	4.9
Belgium	+ 1.5	Q2	+ 1.2	+ 1.3	+ 1.7	– 4.0	Jul	+ 6.7	Jul	13.5	Aug†	13.2
Britain	+ 1.5	Q2	+ 2.0	+ 1.9	+ 2.1	– 1.9	Aug	+ 0.8	Aug	4.7	Jul††	4.7
Canada	+ 2.7	Q2	+ 3.2	+ 2.9	+ 3.0	+ 0.6	Jul	+ 5.9	Jun	6.8	Aug	7.1
Denmark	+ 0.8	Q1	+ 0.6	+ 2.0	+ 2.1	– 1.6	Jul	+ 4.9	Aug	5.7	Aug	6.4
France	+ 1.3	Q2	+ 0.5	+ 1.4	+ 1.6	– 0.7	Jul	– 1.2	Jul	9.9	Aug	10.0
Germany	+ 0.6	Q2	nil	+ 0.9	+ 1.1	+ 3.0	Jul	+ 2.2	Aug	11.7	Sep§	10.7
Italy	+ 0.1	Q2	+ 2.7	nil	+ 0.9	– 0.9	Jul	– 1.6	Jul	7.8	Mar	8.2
Japan	+ 1.4	Q2	+ 3.3	+ 2.2	+ 2.0	+ 1.6	Aug	+ 3.6	Jun	4.3	Aug	4.8
Netherlands	+ 1.3	Q2	+ 4.9	+ 0.6	+ 1.6	+ 0.1	Jul	+ 1.2	Jun	6.6	Aug**	6.2
Spain	+ 3.4	Q2	+ 3.6	+ 3.3	+ 2.9	+ 3.8	Aug	+ 3.1	Aug	9.4	Aug	10.8
Sweden	+ 2.3	Q2	+ 2.6	+ 2.3	+ 2.7	+ 7.8	Jul	+ 6.2	Aug	6.5	Aug†	5.5
Switzerland	+ 1.0	Q2	+ 1.1	+ 1.1	+ 1.6	+ 3.9	Q2	+ 1.6	Jul	3.6	Aug†	3.7
United States	+ 3.6	Q2	+ 3.3	+ 3.5	+ 3.2	+ 3.1	Aug	+ 7.5	Jul	4.9	Aug	5.4
Euro area	+ 1.1	Q2	+ 1.2	+ 1.2	+ 1.5	+ 0.5	Jul	+ 2.0	Aug	8.6	Aug	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 0.2	Q2	– 6.3	na	na	– 3.9	Aug	+ 5.4	Jul	7.2	Aug†	8.0
Greece	+ 3.7	Q2	na	na	na	– 4.5	Jul	+ 3.9	Jun	9.9	Mar	10.8
Iceland	+ 6.8	Q2	na	na	na	na		na		2.0	Jul†	3.0
Ireland	+ 4.1	Q2	+ 6.5	na	na	– 3.2	Jul	+ 4.9	Jul	4.3	Aug	4.4
Luxembourg	+ 3.1	Q1	na	na	na	– 1.5	Jun	– 1.4	Jul	4.5	Aug	4.0
New Zealand	+ 2.6	Q2	+ 4.5	na	na	+ 3.5	Q4	+ 5.9	Q2	3.7	Q2	4.0
Norway	+ 4.8	Q2	+ 5.2	na	na	– 1.3	Jul	+ 5.1	Aug	4.8	Aug‡	4.5
Portugal	+ 0.5	Q2	+ 4.1	na	na	– 0.8	Jul	– 1.9	Jul	7.2	Q2†	6.3

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††May-Jul; claimant count rate 2.8% in Aug.
§EU harmonised rate 9.0% in Jul. **Jun-Aug.

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Prices and wages

Oct 6th 2005
From The Economist print edition

% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2005	2006	latest	year ago	latest	year ago
Australia	+ 2.5 Q2	+ 2.5	+ 2.6	+ 2.7	+ 6.9 Q2	+ 2.8	+ 5.8 Q2	+ 3.0
Austria	+ 2.0 Aug	+ 2.3	+ 2.2	+ 2.0	+ 0.9 Aug	+ 6.3	+ 2.3 Aug	+ 2.0
Belgium	+ 3.2 Sep	+ 2.0	+ 2.5	+ 2.2	+ 1.8 Aug	+ 5.9	+ 2.5 Jul	+ 2.2
Britain	+ 2.4 Aug*	+ 1.3	+ 2.1	+ 2.2	+ 3.0 Aug	+ 2.8	+ 4.2 Jul†	+ 3.8
Canada	+ 2.6 Aug	+ 1.9	+ 2.3	+ 2.4	– 0.4 Aug	+ 5.5	+ 1.4 Jul	+ 1.5
Denmark	+ 2.2 Aug	+ 1.2	+ 1.6	+ 1.9	+ 5.0 Aug	+ 3.1	+ 2.9 Q2	+ 3.1
France	+ 1.8 Aug	+ 2.4	+ 2.0	+ 1.7	+ 2.8 Aug	+ 2.8	+ 2.9 Q2	+ 2.8
Germany	+ 2.5 Sep	+ 1.8	+ 1.9	+ 1.8	+ 1.9 Aug	+ 4.2	+ 1.3 Jul	+ 0.4
Italy	+ 2.0 Sep	+ 2.1	+ 2.2	+ 2.1	+ 3.7 Aug	+ 3.5	+ 2.9 Aug	+ 2.6
Japan	– 0.3 Aug	– 0.2	– 0.1	+ 0.3	+ 1.7 Aug	+ 1.7	– 3.3 Aug	+ 2.8
Netherlands	+ 1.8 Sep	+ 1.0	+ 1.5	na	+ 5.6 Jul	+ 5.2	+ 0.9 Aug	+ 1.0
Spain	+ 3.3 Aug	+ 3.3	+ 3.2	+ 3.1	+ 4.9 Aug	+ 4.4	+ 3.4 Q2	+ 3.1
Sweden	+ 0.6 Aug	+ 0.6	+ 0.7	+ 1.5	+ 4.2 Aug	+ 2.0	+ 2.6 Jun	+ 1.6
Switzerland	+ 1.4 Sep	+ 0.9	+ 1.2	+ 1.2	+ 1.0 Aug	+ 1.5	+ 0.9 2004	+ 1.4
United States	+ 3.6 Aug	+ 2.7	+ 3.2	+ 3.0	+ 5.1 Aug	+ 3.4	+ 2.7 Aug	+ 2.2
Euro area	+ 2.5 Sep	+ 2.1	+ 2.2	+ 1.9	+ 4.0 Aug	+ 3.1	+ 2.3 Q2	+ 2.1
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 0.9 Aug	+ 0.4	na	na	+ 3.8 Aug	+ 1.8	+ 4.0 Q2	+ 3.8
Greece	+ 3.7 Aug	+ 2.7	na	na	+ 5.5 Aug	+ 4.9	na	na
Iceland	+ 4.8 Sep	+ 3.4	na	na	+ 4.6 Sep	+ 5.2	+ 6.7 Aug	+ 5.2
Ireland	+ 2.3 Aug	+ 2.6	na	na	– 1.1 Aug	– 0.4	+ 6.4 Q1	+ 3.9
Luxembourg	+ 2.7 Aug	+ 2.3	na	na	+ 4.2 Jul	+ 9.8	+ 1.6 Jun	+ 2.8
New Zealand	+ 2.8 Q2	+ 2.4	na	na	+ 4.7 Q2	+ 1.5	+ 2.6 Q2	+ 2.3
Norway	+ 1.9 Aug	+ 1.0	na	na	+19.9 Aug	+16.4	+ 3.8 Q2	+ 4.1
Portugal	+ 2.6 Aug	+ 2.3	na	na	+ 4.4 Aug	+ 4.0	– 0.2 Jun	– 0.1

*RPI inflation rate 2.8% in Aug. †May-Jul.

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Economic forecasts

Oct 6th 2005
From The Economist print edition

The Economist poll of forecasters, October averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2005	2006	2005	2006	2005	2006	2005	2006
Australia	2.2/3.0	2.8/3.8	2.6 (2.4)	3.3 (3.2)	2.6 (2.7)	2.7	-4.8(-5.9)	-4.4 (-5.5)
Austria	1.5/2.3	1.6/2.1	1.8 (1.9)	2.0	2.2 (2.1)	2.0 (1.8)	-0.4	-0.6 (-0.3)
Belgium	1.1/1.4	1.3/2.2	1.3 (1.2)	1.7 (1.9)	2.5 (2.4)	2.2 (2.0)	2.8	2.7 (2.7)
Britain	1.7/2.1	1.6/2.4	1.9 (2.0)	2.1 (2.2)	2.1 (2.0)	2.2 (1.9)	-2.4	-2.5 (-2.5)
Canada	2.7/3.2	2.6/3.5	2.9 (2.8)	3.0	2.3 (2.1)	2.4 (2.2)	1.6 (1.4)	1.5 (1.2)
Denmark	1.5/2.4	1.7/2.5	2.0	2.1 (2.2)	1.6	1.9 (1.8)	2.9 (2.1)	2.7 (1.9)
France	1.0/1.6	1.3/2.0	1.4	1.6 (1.8)	2.0 (1.8)	1.7 (1.6)	-0.8(-0.7)	-0.8 (-0.5)
Germany	0.4/1.0	0.7/1.6	0.9	1.1 (1.3)	1.9 (1.7)	1.8 (1.6)	3.7 (3.6)	3.5 (3.4)
Italy	-0.2/0.2	nil/1.3	nil (-0.2)	0.9 (1.0)	2.2 (2.1)	2.1 (1.9)	-1.4(-1.3)	-1.5 (-1.5)
Japan	1.9/2.4	1.0/2.5	2.2 (1.9)	2.0 (1.9)	-0.1	0.3	3.4	3.3 (3.3)
Netherlands	0.5/0.8	1.0/2.0	0.6 (0.5)	1.6	1.5 (1.4)	na na	3.7	3.6 (3.6)
Spain	3.0/3.5	2.6/3.5	3.3 (3.2)	2.9 (2.8)	3.2	3.1 (2.9)	-6.1(-5.4)	-6.0 (-5.5)
Sweden	2.1/2.4	2.3/3.2	2.3 (2.1)	2.7	0.7 (0.5)	1.5 (1.3)	7.1 (6.7)	6.6 (6.2)
Switzerland	0.8/1.3	1.1/2.0	1.1 (0.8)	1.6 (1.5)	1.2 (1.1)	1.2 (1.1)	11.4	10.9 (11.0)
United States	3.3/3.7	2.6/4.0	3.5 (3.7)	3.2 (3.3)	3.2 (3.0)	3.0 (2.7)	-6.5(-6.3)	-6.6 (-6.3)
Euro area	1.0/1.4	1.2/1.8	1.2 (1.3)	1.5 (1.7)	2.2 (2.1)	1.9 (1.8)	0.2 (0.3)	0.2 (0.2)

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, J.P. Morgan Chase, Morgan Stanley, Decision Economics, BNP Paribas, Royal Bank of Canada, Citigroup, Scotiabank, UBS

Every month, *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's figures, where they are different, are shown in brackets. The panel is generally expecting lower growth and higher inflation than a month ago. It has trimmed its growth forecast for America to 3.5% in 2005 and 3.2% in 2006 while raising its inflation projection to 3.2% and 3.0% respectively. It has also cut its growth prediction for the euro area to 1.2% this year and 1.5% next year while raising its inflation forecast to 2.2% and 1.9% respectively. However, the panel now expects Japan to grow by 2.2% in 2005 and 2.0% in 2006, up from 1.9% each year last month.

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Money and interest rates

Oct 6th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Oct 5th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 5.6	+ 8.6	Aug	5.63	5.42	5.26	5.37	5.48	6.31
Britain	+ 6.2	+10.2	Aug	4.53	4.88	4.16	4.26	4.83	5.17
Canada	+ 7.4	+ 9.7	Aug	2.90	2.50	3.33	3.93	4.67	5.15
Denmark	+20.7	+14.8	Aug	2.20	2.21	2.32	3.10	4.04	4.81
Japan	+ 4.4	+ 1.7	Aug	0.02	0.03	0.23	1.50	1.58	1.63
Sweden	+ 2.5	+ 6.2	Aug	1.52	2.05	2.17	3.06	4.24	2.92
Switzerland	+ 0.2	+ 5.6	Aug	0.81	0.71	1.25	1.91	2.57	1.94
United States	+ 1.0	+ 6.1	Aug	3.85	2.00	4.21	4.35	4.22	5.35
Euro area†	+11.5	+ 8.1	Aug	2.18	2.15	2.36	3.14	3.95	3.45

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 4.57%, Japan No. 272 1.51%. Central bank rates: US fed funds 3.75%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Oct 6th 2005
From The Economist print edition

2000=100

	Sep 27th	Oct 4th*	% change on one month	% change on one year
Dollar index				
All items	132.1	133.8	– 0.5	+ 9.5
Food	120.8	123.7	– 0.3	+10.2
Industrials				
All	146.7	146.9	– 0.8	+ 8.8
Nfa†	133.4	135.7	+ 0.3	+10.2
Metals	154.0	153.1	– 1.3	+ 8.2
Sterling index				
All items	113.5	115.2	+ 4.1	+10.8
Euro index				
All items	101.8	103.7	+ 4.0	+12.9
Yen index				
All items	138.9	141.8	+ 3.5	+12.6
Gold				
$ per oz	460.10	465.75	+ 4.9	+12.0
West Texas Intermediate				
$ per barrel	65.04	63.85	– 3.0	+25.0

* Provisional. † Non-food agriculturals.

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Stockmarkets

Oct 6th 2005
From The Economist print edition

Market indices

	Oct 5th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,496.8	4,617.4	3,905.5	- 1.7	- 2.6	+10.9	+ 7.0
Austria (ATX)	3,439.2	3,503.9	2,415.0	+ 0.5	- 1.8	+41.5	+24.4
Belgium (Bel 20)	3,363.3	3,373.8	2,958.8	+ 0.6	- 8.7	+14.7	+ 0.9
Britain (FTSE 100)	5,427.8	5,501.6	4,783.6	- 1.2	-21.7	+12.7	+ 3.4
Canada (Toronto Composite)	10,748.1	11,081.2	9,006.2	- 2.7	- 5.6	+16.2	+17.9
Denmark (KBX)	339.3	341.9	257.8	- 0.1	- 0.8	+31.6	+15.4
France (SBF 250)	3,210.8	3,248.3	2,633.6	nil	-26.9	+21.9	+ 7.2
(CAC 40)	4,594.1	4,650.2	3,816.1	- 0.1	-33.6	+20.2	+ 5.7
Germany (DAX)*	5,069.4	5,138.0	4,178.1	+ 0.4	-37.1	+19.1	+ 4.8
Italy (S&P/MIB)	34,136.0	34,874.0	30,645.0	- 2.1	-31.9	+10.5	- 2.8
Japan (Nikkei 225)	13,689.9	13,738.8	10,825.4	+ 1.9	-64.8	+19.2	+ 7.2
(Topix)	1,409.7	1,428.1	1,109.2	+ 0.6	-51.1	+22.6	+10.3
Netherlands (AEX)	405.0	408.7	347.0	+ 0.7	-42.3	+16.3	+ 2.3
Spain (Madrid SE)	1,168.3	1,176.9	950.9	+ 0.3	- 0.7	+21.8	+ 7.1
Sweden (Affarsvarlden Gen)	271.6	273.7	218.9	+ 0.7	-32.1	+22.8	+ 4.9
Switzerland (Swiss Market)	7,026.4	7,042.3	5,669.6	+ 1.8	-16.5	+23.4	+ 8.3
United States (DJIA)	10,317.4	10,940.6	10,012.4	- 1.5	-12.0	- 4.3	- 4.3
(S&P 500)	1,196.4	1,245.0	1,137.5	- 1.7	-21.7	- 1.3	- 1.3
(NASDAQ Comp)	2,103.0	2,218.2	1,904.2	- 0.6	-58.3	- 3.3	- 3.3
Europe (FTSEurofirst 300)†	1,228.5	1,242.0	1,038.6	- 0.1	-27.9	+17.9	+ 3.7
Euro area (FTSE Euro 100)†	1,043.5	1,056.1	894.4	- 0.2	-32.7	+15.8	+ 1.9
World (MSCI)‡	1,200.8	1,225.6	1,115.0	- 1.1	-17.1	+ 2.7	+ 2.7
World bond market (Citigroup)††	628.5	662.3	626.3	- 0.5	- 5.1	- 5.6	- 5.6

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Oct 6th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Oct 5th	year ago	Currency units per $ Oct 5th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 16.4	Aug	− 43.1	Q2	− 4.8	− 4.4	118.5	112.1	1.32	1.38	2.33	1.58	1.16	+ 0.9
Austria	− 1.4	Jul	nil	Jul	− 0.4	− 0.6	103.9§	104.0	0.84	0.81	1.47	–	0.73	− 2.0
Belgium	+ 15.4	Jul	+ 9.2	Jun	+ 2.8	+ 2.7	104.4§	104.4	0.84	0.81	1.47	–	0.73	− 0.5
Britain	−114.3	Jul	− 23.5	Q2	− 2.4	− 2.5	99.0	98.7	0.57	0.56	–	0.68	0.50	− 2.9
Canada	+ 46.5	Jul	+ 16.3	Q2	+ 1.6	+ 1.5	122.8	114.8	1.18	1.26	2.08	1.41	1.04	+ 1.2
Denmark	+ 9.8	Jul	+ 11.5	Jul	+ 2.9	+ 2.7	105.5	106.1	6.24	6.05	11.0	7.46	5.48	+ 1.8
France	− 27.8	Jul	− 24.1	Jul	− 0.8	− 0.8	106.9§	107.0	0.84	0.81	1.47	–	0.73	− 3.0
Germany	+198.8	Jul	+110.5	Jul	+ 3.7	+ 3.5	104.6§	104.7	0.84	0.81	1.47	–	0.73	− 3.5
Italy	− 7.0	Jul	− 26.0	Jul	− 1.4	− 1.5	76.5§	76.6	0.84	0.81	1.47	–	0.73	− 4.4
Japan	+110.4	Jul	+165.8	Jul	+ 3.4	+ 3.3	84.6	85.9	114	111	201	136	–	− 6.1
Netherlands	+ 40.0	Jul	+ 28.3	Q2	+ 3.7	+ 3.6	103.9§	103.9	0.84	0.81	1.47	–	0.73	− 2.2
Spain	− 90.6	Jul	− 75.2	Jun	− 6.1	− 6.0	77.2§	77.2	0.84	0.81	1.47	–	0.73	+ 0.5
Sweden	+ 21.4	Aug	+ 27.9	Q2	+ 7.1	+ 6.6	96.1	99.9	7.78	7.34	13.7	9.30	6.83	+ 0.8
Switzerland	+ 7.0	Aug	+ 51.4	Q2	+11.4	+10.9	106.3	106.5	1.30	1.26	2.28	1.55	1.14	− 1.0
United States	−730.7	Jul	−749.7	Q2	− 6.5	− 6.6	86.4	86.3	–	–	1.76	1.20	0.88	− 4.1
Euro area	+ 54.3	Jul	+ 10.3	Jul	+ 0.2	+ 0.2	115.0	116.7	0.84	0.81	1.47	–	0.73	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 12.0	Jul	+ 6.4	Jul	na	na	81.5§	81.6	0.84	0.81	1.47	–	0.73	+ 1.3
Greece	− 33.7	Jul	− 15.7	Jul	na	na	59.9§	59.9	0.84	0.81	1.47	–	0.73	− 3.8
Iceland	− 1.1	Aug	− 1.6	Q2	na	na	102.8**	95.4	61.4	71.1	108	73.4	53.9	+ 1.1
Ireland	+ 40.2	Jul	− 3.9	Q2	na	na	94.1§	94.0	0.84	0.81	1.47	–	0.73	− 0.7
Luxembourg	− 4.4	Jul	+ 3.0	Q1	na	na	104.4§	104.4	0.84	0.81	1.47	–	0.73	− 0.8
New Zealand	− 4.0	Aug	− 8.2	Q2	na	na	137.8	133.4	1.44	1.48	2.54	1.72	1.26	+ 3.2
Norway	+ 43.3	Aug	+ 40.8	Q2	na	na	110.6	105.2	6.59	6.73	11.6	7.88	5.79	+ 14.4
Portugal	− 22.3	Jun	− 15.7	Jul	na	na	94.1**	93.6	0.84	0.81	1.47	–	0.73	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, July average. ‡OECD forecast. **IMF, May average.

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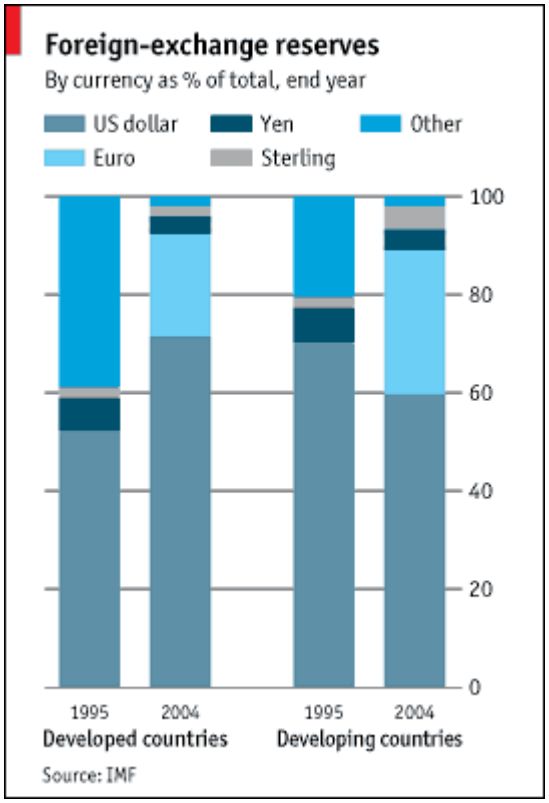
Foreign-exchange reserves

Oct 6th 2005
From The Economist print edition



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Overview

Oct 6th 2005
From The Economist print edition

India's GDP growth accelerated to 8.1% in the year to the second quarter. The country's current-account deficit rose to $16 billion over the same period.

Brazil's trade surplus rose to $41.2 billion in the year to September; **Argentina's** rose to $11.4 billion in the year to August.

Consumer prices in **Venezuela** increased by 15.9% in the year to September.

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Slovakia

Oct 6th 2005
From The Economist print edition

Get article background

Slovakia is the newest member of the OECD and one of its best performers. Its GDP will grow by 5.7% next year, according to the organisation's latest survey of the country. Slovakia has a good chance of meeting the Maastricht convergence criteria for euro entry by 2007, the survey says, allowing it to adopt the single currency in 2009. Despite its vigorous growth and “assertive” labour market reforms, however, the country is still afflicted with a high rate of structural unemployment, which is not helped by the hefty social-security contributions demanded of employers.

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Economy

Oct 6th 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q2	+16.0	Aug	+ 1.3	Aug	+93.1	Aug	+68.7	2004	711.0	Jun
Hong Kong	+ 6.8	Q2	– 0.1	Q2	+ 1.3	Aug	– 9.7	Aug	+21.3	Q2	122.3	Sep
India	+ 8.1	Q2	+ 6.7	Jul	+ 3.4	Aug	–34.7	Aug	–16.0	Q2	133.6	Aug
Indonesia	+ 5.5	Q2	+ 7.3	Jul	+ 9.1	Sep	+27.2	Aug	+ 4.0	Q2	29.9	Aug
Malaysia	+ 4.1	Q2	+ 0.9	Jul	+ 3.7	Aug	+24.1	Aug	+18.0	Q2	79.5	Aug
Philippines	+ 4.8	Q2	– 1.1	Jul	+ 7.0	Sep	– 0.7	Jul	+ 2.9	Mar	15.3	Aug
Singapore	+ 5.2	Q2	+11.8	Aug	+ 0.7	Aug	+17.4	Aug	+32.5	Q2	116.4	Aug
South Korea	+ 3.3	Q2	+ 5.5	Aug	+ 2.7	Sep	+25.2	Sep	+19.9	Aug	206.6	Aug
Taiwan	+ 3.0	Q2	+ 5.9	Aug	+ 3.1	Sep	+ 1.7	Aug	+13.3	Q2	253.8	Sep
Thailand	+ 4.4	Q2	+10.7	Aug	+ 6.0	Sep	– 7.3	Aug	– 2.3	Aug	48.2	Aug
Argentina	+10.1	Q2	+ 6.0	Aug	+10.3	Sep	+11.4	Aug	+ 2.8	Q1	24.4	Jul
Brazil	+ 3.9	Q2	+ 0.5	Jul	+ 6.0	Aug	+41.2	Sep	+12.5	Aug	54.6	Aug
Chile	+ 6.5	Q2	+ 4.5	Aug	+ 3.9	Sep	+ 8.7	Aug	+ 0.6	Q2	15.8	Aug
Colombia	+ 5.3	Q2	– 0.2	Jul	+ 5.0	Sep	+ 1.7	Jul	– 0.8	Q2	14.9	Aug
Mexico	+ 3.1	Q2	– 1.1	Jul	+ 4.0	Aug	– 9.6	Aug	– 8.4	Q2	66.4	Jul
Peru	+ 4.9	Jul	+ 4.6	Jul	+ 1.1	Sep	+ 4.0	Jul	+ 0.4	Q2	12.8	Aug
Venezuela	+11.1	Q2	+ 6.2	Jun	+15.9	Sep	+24.7	Q2	+17.7	Q2	23.1	Jun
Egypt	+ 5.2	Q1	+ 3.3	2004†	+ 4.7	Aug	–10.4	Q2	+ 2.9	Q2	19.0	Aug
Israel	+ 4.8	Q2	+ 3.6	Jul	+ 1.6	Aug	– 7.7	Aug	+ 1.3	Q2	27.8	Aug
South Africa	+ 4.5	Q2	+ 2.4	Jul	+ 3.9	Aug	– 2.4	Aug	– 8.6	Q2	17.2	Aug
Czech Republic	+ 5.1	Q2	+11.2	Jul	+ 1.7	Aug	+ 1.4	Aug	– 4.1	Q2	30.2	Aug
Hungary	+ 4.1	Q2	+ 6.7	Aug	+ 3.6	Aug	– 3.4	Jul	– 8.6	Q2	18.0	Aug
Poland	+ 2.8	Q2	+ 4.6	Aug	+ 1.6	Aug	– 3.3	Jul	+ 0.3	Jul	39.4	Jul
Russia	+ 6.1	Q2	+ 3.4	Aug	+12.4	Sep	+110.6	Jul	+78.3	Q2	146.0	Aug
Turkey	+ 4.2	Q2	– 0.3	Jul	+ 8.0	Sep	–40.4	Aug	–20.0	Jul	41.2	Aug
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.0	Q2	+ 5.5	Aug	+ 4.2	Aug	– 2.3	Jul	– 1.4	Jul	1.8	Jul
Latvia	+11.6	Q2	+ 5.0	Jul	+ 6.1	Aug	– 2.7	Jul	– 1.5	Jul	2.1	Jul
Lithuania	+ 8.0	Q2	na		+ 1.3	Aug	– 3.1	Jul	– 1.4	Jul	3.4	Jul
Slovakia	+ 5.1	Q2	+ 4.7	Jul	+ 2.0	Aug	– 2.0	Jul	– 2.4	Jun	15.3	Jul
Slovenia	+ 5.2	Q2	+ 3.5	Jul	+ 3.2	Sep	– 1.3	Jul	nil	Jul	8.1	Jun
Pakistan	+ 8.4	2005†	+13.6	Apr	+ 8.4	Aug	– 7.3	Aug	– 1.5	Q2	10.6	Jun
Saudi Arabia	+ 5.2	2004	na		+ 0.3	Jul	+84.9	2004	+51.5	2004	24.8	Jul

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Oct 6th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Oct 5th		Dec 31st 2004	
	Oct 5th	year ago	Oct 5th	% a year		one week	in local currency	in $ terms
China	8.09	8.28	14.2	1.95	1,214.0	+2.1	– 8.7	– 6.6
Hong Kong	7.75	7.80	13.6	4.23	15,161.0	–0.4	+ 6.5	+ 6.9
India	44.2	45.8	77.9	5.10	8,724.5	+1.4	+ 32.1	+ 29.9
Indonesia	10,030	9,105	17,665	12.58	1,104.1	+7.4	+ 10.4	+ 2.2
Malaysia	3.77	3.80	6.64	2.91	927.5	+0.3	+ 2.2	+ 3.0
Philippines	55.8	56.3	98.3	7.88	1,940.9	–1.8	+ 6.5	+ 7.1
Singapore	1.69	1.69	2.98	2.34	2,325.9	+1.0	+ 12.6	+ 8.7
South Korea	1,040	1,153	1,831	3.98	1,227.4	–0.1	+ 37.0	+ 36.4
Taiwan	33.2	33.9	58.5	1.55	6,135.0	+3.4	– 0.1	– 4.7
Thailand	41.0	41.4	72.3	4.05	717.2	–0.8	+ 7.3	+ 1.6
Argentina	2.92	2.97	5.13	6.69	1,647.4	–2.4	+ 19.8	+ 22.1
Brazil	2.27	2.83	3.99	19.46	30,163.0	–3.7	+ 15.1	+ 35.0
Chile	527	601	928	4.20	10,113.4	+1.0	+ 12.8	+ 19.1
Colombia	2,293	2,602	4,039	6.76	6,963.1	+2.5	+ 60.2	+ 64.4
Mexico	10.7	11.3	18.9	8.99	15,720.4	–0.9	+ 21.7	+ 26.6
Peru	3.36	3.33	5.92	3.06	5,101.1	+1.4	+ 37.5	+ 34.2
Venezuela	2,799§	2,480§	4,930	14.37	20,473.9	–0.1	– 31.6	– 37.0
Egypt	5.75	6.24	10.13	9.35	47,734.8	–0.8	+ 94.2	+105.0
Israel	4.60	4.47	8.09	3.73	759.6	+1.4	+ 18.0	+ 10.9
South Africa	6.54	6.51	11.5	7.05	16,590.0	–0.3	+ 31.1	+ 13.0
Czech Republic	24.8	25.6	43.6	1.83	1,471.3	+1.4	+ 42.6	+ 28.6
Hungary	209	200	367	6.08	23,215.3	+0.6	+ 57.5	+ 36.4
Poland	3.27	3.52	5.76	4.55	33,708.5	+1.0	+ 26.6	+ 15.9
Russia	28.6	29.2	50.4	13.00	1,009.6‡	+2.2	+ 69.7	+ 64.4
Turkey	1.35	1.51	2.38	15.92	34,775.7	+6.2	+ 39.3	+ 39.1
EM (MSCI)*	1.00	1.00	1.76	na	652.8	+0.4	+ 20.4	+ 20.4
EMBI+†	1.00	1.00	1.76	na	358.2	–0.5	+ 8.7	+ 8.7

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

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